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THESIS

GOVERNMENT FURNISHED PROPERTY:
MANAGEMENT AND ACCOUNTING

by

William Eutis Moore

June 1986

Thesis Advisor:

Willis R. Greer, Jr.

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Government Furnished Property:
Management and Accounting

by

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Submitted in partial fulfillment of the
requirements for the degree of

MASTER OF SCIENCE IN MANAGEMENT

from the

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ABSTRACT

This thesis assesses property management in Department of Defense (DOD) contract administration activities. A brief history of property administration and events which have led to criticism of DOD management and accounting is presented. Acquisition strategy is reviewed to provide perspective and rationale for the use of Government furnished property (GFP). Data was collected from seven contract administration activities through visits and interviews with Property Management Specialists.

The conclusions provide assessments of the system, regulations, organization, and staffing for the management and accounting of GFP. Evidence reveals: low risk for contractor, low organizational visibility for property management and critical shortage of staffing. Recommendations include: a balanced sharing of risk between Government and contractor and a more career enhancing organizational structuring of the property management function within contract administration activities.

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I. INTRODUCTION

A. GENERAL INFORMATION

The Department of Defense (DOD) practice of allowing Government-owned property to be used by private defense contractors has become a source of considerable controversy during the past decade. The issue has centered around the processes involved in managing the acquisition of major defense systems and the role of the Department of Defense in overseeing those processes. Specifically, criticism has been directed at the DOD's methods of managing and accounting for Government property when it is used by defense contractors.

Over the years, service investigations and audits have uncovered numerous incidents of fraud and mismanagement by contractors who were entrusted with Government furnished property (GFP). Investigations by the U. S. General Accounting Office (GAO) confirmed these abuses and concluded that their primary cause was lack of sufficient controls at the DOD level in providing for effective contract management.

Under established defense acquisition regulations, the DOD has relied primarily upon the contractor's records for the accountability and control of government furnished property. Unfortunately, this process has allowed many unscrupulous or inefficient contractors to use the system to their own advantage. Reports have shown that GFP has been requisitioned in excess of contract needs; it has been retained in excess after completion of work; it has been used for commercial contracts; and, it has even been sold back to the Government after use. These reported abuses have given rise to

substantial, unnecessary costs to the Government and have seriously brought into question the credibility of DOD's management systems.

Although the Federal Acquisition Regulation (FAR) establishes the general policy that contractors will furnish all property, the Government may still furnish its own property to a contractor by reason of economy, standardization, expediency of production, nonavailability of commercial sources, or other appropriate condition, particularly in regard to industrial mobilization. [Ref. 1: pp. 13-4 to 13-16] Despite this apparently prudent policy, DOD estimates of the cost of Government property currently in the hands of contractors is almost \$40 billion. [Ref. 34: pp. 2 - 5]

Because of these large amounts of GFP in use, reported abuses and alleged mismanagement have attracted intensive scrutiny from Congress and the news media. Congressional investigations during the past six years have brought stern admonishments and counselling from Congressional leaders regarding improvement of DOD's methods of control over Government furnished property in the hands of contractors.

[Ref. 34: pp. 11 - 16]

To Congressional investigators, DOD's response has been slow and unsatisfactory. Recurring reports of newly discovered abuses only serve to heighten Congressional skepticism of DOD competence in this area. Nevertheless, DOD initiatives to implement reforms have been well received by some members of Congress. Also, industry leaders have undertaken programs to reform from within and to assist DOD in the enforcement of established regulations and standards.

As major acquisition programs mature and begin to phase-out, the problem of managing GFP will obviously subside with fewer and fewer of

these assets remaining in the system. Also, as the total dollar amount of GFP diminishes, it is reasonable to expect that its relative importance as a political issue will also fade. Politics notwithstanding, whether defense acquisition managers have solved the problem of managing and accounting for GFP is still a question worth asking. If the answer is negative, then expectations for the next major expansion of defense acquisitions should be that these same kinds of problems will recur in the management and accounting of Government owned property in the hands of contractors.

B. OBJECTIVES

The objectives of this study are to analyze and assess the systems currently used to manage and account for the two types of GFP which are the largest and most difficult to control: material and equipment. With a better understanding of these systems and their actual employment, a more accurate determination concerning the adequacy of management and accountability can be made. Having thus established a firm foundation through closer assessment, the development of improved alternatives will be explored.

C. RESEARCH METHODOLOGY

The research methodology of this study consists of a comprehensive review of historical literature; analysis of regulations concerning use and accountability of GFP; telephone interviews with professionals involved in the process of managing GFP; and on-site interviews with personnel working in jobs involving Government property administration.

The literature was accumulated through the Naval Postgraduate School, the Defense Logistics Studies Information Exchange (DLSIE), and the Defense Technical Information Center (DTIC).

Personal and telephone interviews were held with both past and present senior executive managers of acquisition programs and policy, contract administrators, audit and Inspector General personnel, Government property administrators and industrial property administrators working on contracts for each of the three services.

Regulatory data was taken from the Federal Acquisition Regulation (FAR), Defense Acquisition Regulation (DAR), Armed Services Procurement Regulation (ASPR), GAO and service comptroller guidelines, and contract administration procedures.

D. SCOPE OF STUDY

The scope of this study was limited to an assessment of the policies and procedures used for managing and accounting for Government furnished material (GFM) and equipment (GFE) used in the acquisition of defense systems and the purchase of components and assemblies for these systems.

Although strategy issues are presented, no attempt was made to evaluate the decision-making process concerning the selection of government furnishings as an acquisition strategy. Rather, this study assesses the effectiveness of documenting, monitoring, tracking and valuing GFM and GFE in acquisition programs after the decision to use them has been made.

E. DEFINITIONS

The following definitions and terms are applicable to concepts used in this study:

1. **Property** includes all property, both real and personal. It consists of five separate categories -- material, special test equipment, special tooling, military property and facilities. [Ref. 1: p. 13-101.1]
2. **Government property** means all property owned by or leased to the Government or acquired by the Government under the terms of a contracts defined below:
 - a. **Government-furnished property** is property in the possession of, or acquired directly by, the Government and subsequently delivered or otherwise made available to the contractor; and,
 - b. **Contractor-acquired property** is property procured or otherwise provided by the contractor for the performance of a contract, title to which is vested in the Government.
[Ref. 1: p.13-101.2]
3. **Material** means property which may be incorporated into or attached to an end item to be delivered under a contract or which may be consumed or expended in the performance of a contract. It includes, but is not limited to, raw and processed material, parts, components, assemblies, and small tools and supplies which may be consumed in normal use in the performance of a contract.
[Ref. 1: p. 13.101.4]
4. **Special test equipment** means either single or multipurpose integrated test units engineered, designed, fabricated, or modified to accomplish special purpose testing in the performance of the contract. Such testing units comprise electrical, electronic, hydraulic, pneumatic, mechanical, or other items or assemblies of equipment, that are mechanically, electrically, or electronically interconnected so as to become a new functional entity, causing the individual item or items to become interdependent and essential in the performance of special purpose testing in the development or

production of particular supplies or services. The term "special test equipment" does not include:

- a. material;
- b. special tooling;
- c. buildings and nonseverable structures; and,
- d. plant equipment items used for general plant testing purposes.
[Ref. 1: p. 13-101.6]

5. **Special tooling** means all jigs, dies, fixtures, molds, patterns, taps, gauges, other equipment and manufacturing aids, and replacements thereof, which are of such a specialized nature that, without substantial modification or alteration, their use is limited to the development or production of particular supplies or parts thereof, or the performance of particular services. The term includes all components of such items, but does not include:

- a. consumable property (material);
- b. special test equipment; or
- c. buildings, nonseverable structures, general or special machine tools, or similar capital items. [Ref. 2: p. 45-1]

6. **Facilities** means industrial property (other than material, special tooling, military property, and special test equipment) for production, maintenance, research, development, or test, including real property and rights therein, buildings, structures, improvements, and plant equipment. [Ref. 1: p. B-102.7]

7. **Military Property** means Government owned personal property designed for military operations. It includes end items and integral components of military weapons systems, along with the related peculiar support equipment which is not readily available as a commercial item. It does not include Government material, special test equipment, special tooling or facilities. [Ref. 1: p. 13-101.7]

8. **Property Administrator** is the individual designated by appropriate authority to administer the contract requirements and

obligations relative to Government property. This person is an authorized representative of the contracting officer.

[Ref. 1: p. B-102.1]

9. **Component** is a subsystem, assembly, sub-assembly or other major element of an end item. [Ref. 1: p. 1-326.2]
10. **Component Break-out** is the process separating certain components or subsystems of the end-product from the contract with the prime contractor. The components or subsystems are then obtained from another source and supplied to the prime contractor as Government furnished property for integration into the final system. The alternate sources may be other acquisition programs, other vendors or DOD supply systems.
11. **Component Break-in** is the process which adds components and subsystems which were previously furnished by the Government to the contractor's production requirements. The contractor may buy these components and subsystems from a subcontractor or from the Government.
12. **Real property**, for purposes of accounting classification, means (i) land and rights therein, (ii) ground improvements, (iii) utility distribution systems, (iv) buildings, and (v) structures. It excludes foundations and other work necessary for the installation of special tooling, special test equipment and plant equipment.
[Ref. 1: p. B 102.8]
13. **Category** means a segment of a contractor's property control system, i.e., acquisition, receiving, records, storage and movement, consumption, utilization, maintenance, physical inventories, subcontractor control, and disposition. [Ref. 24: p. S3:1]
14. **Contracting Officer** is a term used to describe the contracting representative in each of two interdependent facets of the contracting process: [Ref. 32: pp. 2-13, 2-14]
 - a. **Procurement Contracting Officer (PCO)** is the official Government representative in contracting process responsible for all activities associated with the award of the contract. The PCO signs the contract and only the PCO can authorize changes to

it. The PCO must ensure that the contracts are legal and that they protect the interests of the Government.

- b. **Administrative Contracting Officer (ACO)** is the on-site representative of the contract administrative services office and acts on delegated authority from the PCO. The ACO provides pre-contract information such as cost/price data, contractor property management system information, strengths and weaknesses of the contractor's proposals, etc..

15. **Plant clearance** means all actions relating to the screening, redistribution, and disposal of contractor inventory from a contractor's plant or work site. [Ref. 2: p. 45-20]

16. **Plant Clearance Officer** means an authorized representative of the contracting officer assigned responsibility for plant clearance. [Ref. 2: p. 45-20]

II. HISTORY OF GFP

Governmental agencies have been furnishing property in the form of material and equipment to contractors since the early 1930's. Then, the Government not only managed the acquisition of GFM and GFE but would also integrate the GFM/GFE into the weapon system being manufactured. However, as systems became increasingly more complex and the integration process became more and more difficult, the DOD recognized that it possessed neither the technical nor the administrative resources necessary to carry out this responsibility. Consequently, by the 1950's, the concept of having the prime contractor integrate the GFM/GFE became accepted practice.

Likewise, as systems grew even more complex, prime contractors, too, increasingly began to purchase components from specialty subcontractors who were more efficient than the prime at producing certain subsystems. The prime would buy from the subcontractor and then apply his own engineering and administrative expenses plus a profit margin to the price paid by the Government for the final end-product. By the end of the 1950's, major weapons programs began to mature and the prime contractor's role began to diminish in importance even more.

It was at this time that a program for Army ordnance took advantage of the situation and began "breaking-out" components previously subcontracted by the prime. The Army's subsequent success in reported savings led the Congress to insist that the Navy and Air Force initiate their own break-out programs. [Ref. 3: p. 103]

Interestingly, while component break-out was receiving enthusiastic Congressional endorsement and Secretary of Defense (Robert MacNamara) support, other high ranking officials were expressing reservations. For example, Mr. Graemme C. Bannerman, Assistant Secretary of the Navy, Installation and Logistics, stated in 1965:

The subject needs a very careful examination and there is serious question as to whether it is a good policy. I think it is clear that there are some items we should furnish to the contractor where we have far better buying power than he has, or we have standardization across a whole group of equipments. But we could get into the business of buying his nuts and bolts for him if we went too far with this. And I think, clearly, we do not want to do that.

You have to remember that one of the reasons we hired him was because he could produce a piece of equipment and guarantee us results. Well, to the extent we furnish the pieces of that equipment to him, his guarantee is diluted.

If we are going to be furnishing hundreds of items to him and he is working against a production schedule, every time his production schedule slips, he blames us because some piece of GFE did not show up at the right time. [Ref. 4]

By the early '70's, evidence of component break-out as a practice began to diminish. Some examples were: the Air Force's F-15 project, the Army's Blackhawk Helicopter and the Navy's F-14 program -- all of which demonstrated minimal break-out activity.

In the middle '70's, a whole series of "break-out audits" were conducted to determine the extent of the 'services' compliance with DOD's break-out policy.

In 1975, an Army Audit Agency report showed the U. S. Army Aviation Systems and Missile Commands were not fully implementing their break-out programs and had not realized significant savings through the use of GFM. The audit recommended stronger involvement by the Army's Material

Command. The audit agency, however, did not mention the risks involved and the added costs of managing the program. [Ref. 5]

In 1976, a similar audit conducted by the U. S. Air Force Audit Agency found that the F-15 program officer had not identified all components with break-out potential, had not adequately prepared items for break-out and had not sufficiently documented the need to defer break-out of twelve candidate items determined suitable as GFM. [Ref. 6: p. 28]

Based on the findings of these audits, the House Appropriations Committee concluded:

These audit reports demonstrate that too little attention is being devoted to the component break-out program. _The component break-out program should be applicable across every item of equipment built for the military department, as well as for the spares support purchased for those equipments.
[Ref. 7: p. 266]

The committee went on to cajole the Secretary of Defense to give his attention to the operation of the break-out program in the military departments. [Ref. 7: p. 266]

In 1981, the DOD's management of GFM again came under scrutiny by the House Subcommittee of the Committee on Government Operations, led by Representative Jack Brooks. The subcommittee had obtained reports from the GAO, DOD and service auditors which pointed out mismanagement and contractor abuses, such as:

- Use of Government property for commercial purposes without the consent of the contract administrators.
- Acquisition of property without contractual authority.
- Issuing property in excess of contractual needs.

- Selling Government property back to the DOD.
- Accounting procedures and responsibility definitions sorely inadequate. [Ref. 8: p. 12]

On September 30, 1980, the services had conducted an accounting of GFM actually in contractor possession. The data showed that \$11.2 billion was in the system. The GAO, however, strongly disputed that figure during the 1981 hearings, saying that the amount was much larger and that the services' accounting systems were incapable of accurately estimating GFE in the system at any given time. Even if the accounting systems could process an estimate, the GAO contended, the contractors were often not properly recording inventories of Government property anyway. [Ref. 7: p. 4]

Congressman Brooks concluded the hearings by saying that the DOD did not have an adequate system for insuring sound management of the material it provided to contractors and that subcommittee reviews would continue until confidence was gained that sound systems of control and accountability for GFP were in place. [Ref. 7: p. 85]

On November 2, 1983, the issue of control and accounting procedures for GFM again came before Congressional review in connection with hearings on the purchasing of spare parts and support equipment. Although the issue dealt primarily with overpricing, the fact that DOD had still not established effective contract auditing procedures and that contractor abuses were still occurring, led the Committee on Governmental Affairs Chairman, Senator William Roth, to call for tighter controls, more effective auditing and better evaluative accounting. [Ref. 8: pp. 119,120]

In 1985, new House of Representatives hearings were convened to follow-up on the October 1, 1981 hearings. Representative Brooks,

remaining true to his word, opened fire on perceived inadequacies of GFM management and the DOD's apparent unwillingness to improve its accountability systems. [Ref. 9: pp. 5 - 8] The subcommittee had made seven specific recommendations to the DOD in 1981 and had assiduously monitored their progress through the GAO since then: [Ref. 9: pp. 28 - 32]

Recommendation 1: DOD should place the responsibility for coordinating all actions planned and underway for improving management and accountability for GFM in one adequately staffed central office.

DOD agreed that GFM management needed to be coordinated among the three services, but considered it impractical to assign that function to a single office because it would pull expertise away from other property administration efforts such as logistics and acquisition.

Rather than a central office, DOD established a Defense Government Property Council (DGPC) in April 1983. The council is responsible for managing all Government property, including GFM and GFE. The council created a coordination committee and eight ad hoc groups to deal with the various property issues. Senior Executive Service (SES) officials of the DOD and the services are assigned to the council and ad hoc groups. The specified missions of this council are:

- Insure effective overall management of Government property at contractor plants.
- Serve as a focal point to address Government property issues.
- Provide continuing oversight and policy direction in Government property management.

- Insure that the organization, staffing and functioning of property management are commensurate with efficient and quality results. [Ref. 10]

Recommendation 2: DOD property administrators should enforce the provisions of contracts in accordance with the Defense Acquisition Regulation and should periodically check the GFM for losses and excesses.

In April 1984, DOD asked the services and the Defense Logistics Agency (DLA) to implement the recommendation and a review was made of major contracts, all contractors, the contract administration offices, and logistics procedures to ensure compliance.

Recommendation 3: DOD should develop a plan of action as soon as possible to install accounting controls over GFM within DOD and get the applicable systems approved by GAO.

DOD established principles and standards for accounting for GFP, including GFM, and, in 1983, issued them to the services. Full implementation of these standards is not expected to occur until 1989.

Recommendation 4: DOD should involve as many contractors as feasible to test the practicability of selling material to contractors instead of providing GFM.

A test of this concept was completed in October of 1983 which indicated that the sale of GFM to contractors would put all but the smallest contract financially out of reach of small businesses. A report of the test also concluded that more personnel would be required by the contractor and that prices would have to be increased to include the cost of material plus overhead and general and administrative costs of handling.

Recommendation 5: DOD should review the various GAO and DOD audit reports relating to GFM and should implement the recommendations contained therein. In particular, DOD should

systematically review its major GFM contracts to identify and excess material and the finding should be validated.

Completion of implementation of the DOD Inspector General's recommendations for determining excess GFM at contractor plants is expected to be completed by July 1986.

Recommendation 6: DOD should increase the number of property administrators assigned to contractor plants.

In August 1984, the DLA member of the DGPC's Coordination Committee reported that DLA had fully staffed its major maintenance plants with resident property administrators. Also, the total number of Industrial Property Management Specialists and Industrial Property Clearance Specialists have increased from 695, in 1981, to 862 as of September 30, 1984.

Recommendation 7: DOD should control production contractor's access to DOD's supply system.

In March 1981, DOD Instruction 4140.48, "Controls of Access to DOD Material Inventories by Maintenance Contractors," was issued requiring maintenance contractors to submit all requisitions to a central office for review and validation. This instruction is expected to be fully implemented by June of 1986.

Interestingly, on 4 April, 1985, the Navy Government Property Council was created to parallel the DGPC. Its purpose is to provide executive guidance and direction in the management of all government property in the Navy with an additional goal of developing an improved, standardized automatic data processing system for administering Navy property. The other services have yet to follow suit in establishing a single ad hoc group responsible for only government property administration.

On March 20, 1986, the Legislation and National Security Subcommittee, chaired by Representative Jack Brooks met again, this time to examine the DOD's longstanding policy of minimizing the amount of GFE provided to DOD contractors -- noting that GFE in use had increased from \$5.3 billion in 1971 to \$8.4 billion in 1984. At that hearing, Mr. John A. Mittino, Deputy Assistant Secretary Defense (DASD) (Production Support) gave a comprehensive statement of the progress of the DOD in the management and accounting of Government property. A complete transcript is provided in Appendix B.

Mr. Mittino's statement described efforts taking place in essentially three different areas:

- An Industrial Modernization Incentive Program (IMIP)
- Facilities "Phase Down" Policy, including negotiated sale of Government properties.
- Improved Property management through Government Property Councils and implementation of financial accounting standards for property.

The subcommittee concluded its hearings with a shift in emphasis away from GFM toward Government owned, contractor operated (GOCO) facilities and phase down of GFE. The Army was criticized for its operation of GOCO ammunition and tank plants, while DASD (Production Support) received admonishment for lack of uniform enforcement of phase down policy.

Nearly five years have passed since the subcommittee first called for reform in the administration of Government property. The problem, however, seems as yet unsolved.

III. GOVERNMENT FURNISHED PROPERTY IN ACQUISITION STRATEGY

This section provides an introduction to the acquisition process and key policy evolution which has shaped and given substance to major acquisition programs. The acquisition strategy which accompanies this process is very briefly reviewed to indicate key areas of concern in which GFP should be included. Lastly, an overview of the DOD Contract Administration Services system is presented to provide orientation to the environment in which GFP management and accounting takes place.

A. MAJOR SYSTEM ACQUISITION PROGRAM MANAGEMENT

The essential precepts governing DOD acquisition policy include:

1. The requirement that all purchases be made on a competitive basis to achieve maximum innovation and minimum cost.
2. The requirement to express needs in terms of mission rather than in terms of systems needs.
3. The establishment of clear lines of responsibility, authority and accountability for program management.
4. The requirement for approval at key decision points by the responsible department head.
5. The requirement that total life-cycle costs be balanced against system performance, logistic supportability and production schedule. [Ref.: Appendix A]

Acquisition policy is the product of a long evolutionary process which has sought to provide an effective structure for the management of acquisition programs. Generally, progress has been achieved through the

experience and knowledge gained from past successes and failures. The following section provides a brief description of more recent policy advances.

1. Policy Development

Since 1961, and following enactment of the Defense Reorganization Act of 1958, the Secretary of Defense has had a dominant role in program and budget matters in the Department of Defense. His power in the overall process of determining resources for defense, however, is restrained by the Congress and other Executive agency influences. The Secretary of Defense uses the Planning, Programming, and Budgeting System (PPBS) as the primary management mechanism for developing programs and determining defense budgetary needs. [Ref. 12: pp. 13-14]

To study the huge acquisition effort during the Vietnam Era, Congress established, in 1969, the Commission on Government Procurement (COGP). The COGP was to recommend methods that would promote the economy, efficiency and effectiveness of Federal procurement by the Executive Branch. [Ref. 13: all] In all, the COGP made 149 recommendations of which twelve involved improvements to major system acquisition. [Ref. 14: all].

Following one of the recommendations of the COGP, the Office of Federal Procurement Policy (OFPP) was established within the Office of Management and Budget (OMB). OFPP was charged with developing and establishing procurement policies across all Executive Branch agencies. After two years of joint Legislative and Executive effort, policy guidelines in the form of OMB Circular A-109 were issued in April of 1976. (See Appendix A.) The circular incorporates the key elements of the twelve recommendations

of the COGP and provides to all agencies a standardized approach for the establishment of acquisition policy and program implementation.

The primary purpose of A-109 is to promote competition throughout all phases of the acquisition process. It is also intended to focus competition upon early phases, to provide a broader base for competition, to require a more sequacious commitment of resources, and to foster innovation. A key element of this process is the requirement that all agencies express needs and program objectives in mission terms rather than equipment terms to encourage creating, exploring and developing alternative systems.

To further amplify the intent of Circular A-109 and to establish important decision points through a major systems acquisition cycle, OFPP issued a pamphlet which described the process as a single closed loop with four key decision points after each of four phases. These four key decisions are to be made by the agency head:

- a. Identification of mission need,
- b. Selection of competitive system design or single concept,
- c. Full scale development and limited production, and
- d. Commitment to full production. [Ref. 14: all]

A-109 also states that an acquisition strategy should be developed and tailored as soon as the agency decides to solicit alternative system design concepts that could lead to the acquisition of a new major system and, also, that steps should be taken to refine the strategy as the program proceeds through the acquisition process. [Appendix A: p. 5.]

As a consequence of this guidance, it is now the practice of all services to develop an acquisition strategy early in the Concept Exploration phase after the program initiation. This policy has been translated through

Department of Defense Directive 5000.1 and Department of Defense Instruction 5000.2 . Each of the services now have their own implementing regulations. [Refs. 15, 16, 17, and 18: all.]

Although the circular and the Federal Acquisition Regulation (FAR) describe in general terms what the strategy considerations should be, each of the military departments has addressed this requirement in its own way. This has led to some variation in the guidance regarding content, format and important issues to be used. Table III-1 is a summary of the major areas considered critical by the DOD, Federal and service levels. It is noteworthy for this study that only the FAR and DAR specifically address Government furnished property as a key element.

In 1984, the FAR became the sole regulatory document for acquisition, superseding the DAR. However, many contracts and management systems which came under the old regulations are still functioning. Thus, working cross-references are still maintained by both administrators and contractors. Agency regulations unique to DOD are now included in a FAR supplement called Defense Federal Acquisition Regulation Supplement (DFARS).

Under Title VII of the Spending Reduction Act, Deficit Reduction Act of 1984, a considerable number of changes and amendments relating to competition in contracting were made to the Armed Services Procurement Act, Federal Property and Administrative Act, Office of Federal Procurement Policy (OFPP) Act and the GAO Procurement Protest System.

These changes have had far reaching effect upon the FAR and they are still being implemented into the regulation at this date.

2. The Acquisition Process

The acquisition process is conceptually quite simple, however, the detail of its specific requirements is very complex. The fundamental process involves four separate phases: Concept Exploration, Demonstration and Validation, Full Scale Development and, lastly, Production and Deployment.

The actual origins of a system acquisition cannot be precisely identified. Rather, it manifests slowly from the services' operational experience, from advances in the technology base, and from an evaluation of the potential threat. When a need is ultimately perceived, that need is prioritized along with all others in consideration of the agency's goals, resources and existing capabilities. As the concept gains advocacy through internal influences, an initial justification document or tentative operational requirement statement is submitted into the Planning, Programming and Budgeting System (PPBS) for consideration. Once within the (PPBS), the initial budget document must compete with all other proposals for available funds. In some cases, the Concept Exploration phase may not begin until the funds have actually been appropriated. This could be as long as two years after the initial operational requirement was submitted. [Ref. 19: encl 4] and [Ref. 20: pp. 13-21]

TABLE III-1, PART 1:

GUIDANCE ON ACQUISITION STRATEGY AND PLANNING

| ELEMENTS OF A-109 ACQUISITION STRATEGY | ELEMENTS OF FAR ACQUISITION PLANNING (PART 7) | ELEMENTS OF DAR PROCUREMENT PLANNING (PART 21) |
|---|---|---|
| <ul style="list-style-type: none"> - Contracting Process - Scheduling of Essential Elements - Demonstration Test and Evaluation Criteria - Content of Solicitation for Proposals - Decisions On Whom To Solicit - Methods for Obtaining, Sustaining Competitors - Guidelines for Evaluation and Acceptance/Rejection of Proposals - Goals for Design-to-cost - Methods for projecting Life Cycle Costs - Use of Data Rights - Use of Warranties - Methods for Analyzing, Evaluating Contract Government Risks - Need for Developing Contractors Incentives - Selection of the Type of Contract Best Suited for Each Stage of Acquisition - Administration of Contracts | <ul style="list-style-type: none"> - Acquisition Background and Objectives - Statement of Need - Environmental Concerns - Requirement for Compatibility With Existing or Future Systems/Programs - Cost, Schedule, Capability, Performance Constraints - Security Considerations - Milestones - Life-cycle cost - Design-to-cost - Application of Should-cost - Capability or Performance - Delivery or Performance-Period Requirements - Trade-offs - Risks <ul style="list-style-type: none"> Plan of Action - Sources - Competition - Source-Selection Procedures - Contracting Considerations - Auth. for Contracting by Negotiation - Budgeting and Funding - Product Descriptions - Allocations, Allotments - Contractor vs Government Performance - Management Information Requirements - Make or Buy - Test and Evaluation - Logistics Considerations <ul style="list-style-type: none"> -- Contractor/Agency Support -- Reliability, Maintainability, Warranties, QA -- Contractor Data Needs - GFP (property) - GFI (information) - Participants | <ul style="list-style-type: none"> - Description of Program, Item, or System - Program Funding - Delivery Requirements both R&D and Production Contracts - Applicability of Decision Coordinating Paper, Program Memorandum, Defense System Acquisition Review Council, or Internal Service Review - Background - Discussion of Program Technical, Cost, and Schedule Risks - Integrated Logistics Support Planning Concept - Application of Design-to-cost - Application of Life-Cycle Cost - Reliability, Maintainability, Warranties - Test and Evaluation - Management Information Requirements - Approval for Operational Use - GFP/Component Break-out - Application of Should-Cost - Milestone Chart - Milestone Updates - Participants - Procurement Approach for each Contract |

TABLE III-1, PART 2

GUIDANCE ON ACQUISITION STRATEGY AND PLANNING

ELEMENTS OF NAVY
ACQUISITION STRATEGY
(SECNAVINST 5000.29A)

- Section I: Needs, Constraints, Thresholds, and Program Structure
 - Statement of Need
 - Program Constraints and/or thresholds
 - Resources and Funding
 - Program Structure
- Section II: Risk Analysis
- Section III: Strategy to Achieve Objectives and Implementation
 - Objectives and goals
 - Program Schedule
 - Acquisition Alternatives
 - Decision Plan
 - Coordination with other Programs
 - Risk Management
 - Product Improvement
 - Preplanned Product Improvement
 - Design and Manufacture Reliability
 - Standardization
 - Design-to-Cost
 - Integrated Logistics Support Approach
 - Use of Organizational Assets
 - Mobilization Capability
 - Financial Strategy
 - Funding for Testing Hardware
 - Business Management Approach
 - Audit Trail of Key Decisions

ELEMENTS OF AIR FORCE
PROGRAM MANAGEMENT
PLAN (AFR 800-2, 3)

- Program Summary and Authorization
- Intelligence
- Program Management
- System Engineering
- Test and Evaluation
- Communication and Electronics
- Operations
- Civil Engineering
- Logistics
- Manpower and Organization
- Personnel Training
- Security
- Directives Applications

ELEMENTS OF ARMY
ACQUISITION STRATEGY
(AR 70-1)

- Program Structure
- Contracting Strategy
- Tailoring the Acquisition Process
- Supportability
- Manufacturing and Production
- Test and Evaluation
- Cost Growth
- Technical Risks
- Safety and Health

ELEMENTS OF RECENT
ACQUISITION
PLAN

- Program Description
- Program Funding
- Delivery Requirements
- Applicability of Decision Coordinating Paper and Defense Systems Acquisition Review Council Reviews
- Background and Acquisition History
- Program Risks
- Integrated Logistics and Support Planning
- Application of Design-to-Cost
- Life-Cycle Costing
- Reliability, Maintainability, Quality Goals
- Test and Evaluation
- Management Information Systems
- Approval for Full Production
- GFP/GFE/GFM**
- Should-Cost
- Industrial Preparedness Planning
- Acquisition Milestones
- Schedule for Updating Acquisition Schedule
- Acquisition Plan Participants
- Contracting Approach
- Long Range Plan

[Ref. 21: pp. 1-4, 1-5]

a. Concept Exploration (CE)

The CE phase of the acquisition process searches among all identifiable alternatives and then endeavors to obtain the knowledge base necessary to select the best alternatives for system concepts and hardware/software development. The technical specifications and economic bases for proposed systems are established through applied studies and the evaluation of experimental concepts. Analyses of support and readiness criteria of current systems, targets for new systems, development of alternative operational and support concepts, evaluation of manpower and logistic support requirements must all be thoroughly developed during this initial stage of acquisition. All critical issues are identified for resolution in the subsequent phases in an attempt to ensure that future development risks are minimized.

It is in this first phase of conceptual exploration that initial consideration for the opportunities of using GFP will be made. If the concept involves the furnishing of GFP, then logistic support requirements must be determined, for the costs involved in the added administrative workload of managing and accounting for GFP can easily exceed any anticipated savings. Likewise, due consideration must be given to the contractual clauses which specify the terms of GFP use.

The outputs of the CE phase consist of a test and evaluation master plan, at least two competing concepts (unless sole-source is required), proposed follow-on contracts and the decision by the agency head to proceed to the Demonstration and Validation Phase.

b. Demonstration and Validation Phase (D & V)

The decision to proceed with development marks the beginning of the D&V Phase. During this phase, test, evaluation and hardware fabrication must confirm that the risks and uncertainties for at least one of the competing concepts can be identified and reduced to acceptable levels. A determination is made concerning the possession of necessary technology so that development can move from exploratory to engineering efforts. Performance criteria for the system are defined and an analysis of cost versus capabilities is made. Techniques for overcoming the effects of uncertainty are refined and implemented. Contracts are written for competitive demonstrations of concepts. Training plans are written as well as plans for maintenance and reliability, logistics support, life cycle costs, safety and survivability development. Competing systems are compared to existing systems and those in development elsewhere. Also, budgeting projections are more accurately refined and used to improve business decision-making.

In the D&V phase, a review is conducted to determine to what extent, if any, the contractors will need support. Thus, the first formal decisions will be made concerning GFP, primarily in the form of laboratories and test equipment. Subsystems and components suitable for possible breakout for competitive procurement or provision as Government furnished material (GFM) or equipment (GFE) are identified. In addition, the need for long lead-time items, materials and facilities is reviewed in preparation for full-scale development.

c. Full-scale Development Phase (FSD)

FSD is a period of careful, iterative and exhaustive engineering design and testing. Heavy use of prototypes and pilot systems is made for the purpose of demonstrating and documenting a cost-effective, reliable and operationally effective system that meets the approved mission need. Deployment plans and logistics support plans are also finalized in this phase. Technical and operational evaluations must be conducted and satisfactorily passed before approval to begin production is issued. Once validation of all acceptance criteria is complete, approval is given to conduct a readiness review and commence a product improvement program. After the contractor has demonstrated adequate capability to manufacture the system and has accumulated the necessary resources to sustain the expected production rate, accomplish necessary rework, and provide spares, the process enters the production phase.

d. Production and Deployment Phase

The activities of the Production and Deployment phase are directed to putting the new product into the field and providing complete support for its successful operation. Quality assurance, configuration control, and failure correction are key issues. However, it is also during this phase that it becomes appropriate to enhance the competitive nature of the process through the location of second sources; possible component or subsystem breakout; and, the use of Government furnished property.

The smooth introduction of new systems and the retirement of old programs must be predicated upon careful and detailed planning. The training of qualified personnel and the installation of support facilities are imperative to successful system implementation. However, planning for

operational support is all too often incomplete, particularly in the area of funding for training and spare parts.

Funding is also of great concern in using GFP during this phase of acquisition because with the increasing complexity of modern systems, the risks and costs involved in managing Government furnishings become more significant. Late or defective GFE, for example, can slow the contractor's production schedule, increase his costs and result in extra expense and delay to the procuring agency.

3. Contract Administration

The acquisition process includes solicitation for offers by potential contractors, the negotiation of the contracts, and, finally, the award of the contracts. Once the contracts are signed, the process of contract administration begins for the Government. By its multiplicity of functions and length of involvement, contract administration has come to represent a major field in procurement and a vital element in the delivery of defense materiel.

The focal point for the administration activity is the contractor's plant and the objective is ensuring satisfactory contract performance. The contract administration office includes a team of specialists who perform the following duties:

- Review contractor's compensation structure.
- Establish final overhead rates and billing rates.
- Negotiate prices and execute supplemental agreements for spare parts and other items selected through provisioning procedures.
- Consent to the placement of subcontracts.

- Monitor contractor's financial condition.
- Conduct postaward orientation conferences.
- Perform property administration and preaward surveys.
- Perform engineering surveillance to assess compliance with contractual terms for schedule, cost and technical performance in the area of design, development, and production .
- Evaluate for adequacy and perform surveillance of contractor engineering efforts and management systems.
- Review and evaluate for technical adequacy and perform surveillance of contractor engineering efforts and management systems.
- Monitor contractor value-engineering program.
- Perform quality assurance. [Ref. 11: p. 80]

The Department of Defense Contract Administration Service (DCAS) has nine regional offices which provide contract administration services under the organization of the Defense Logistics Agency (DLA). The services of DCAS components may be utilized by other U. S. Government Departments, agencies and corporations by direct request. [Ref. 22: all]

The DOD attempts to make maximum use of the DCAS offices to ensure standardized contract administration throughout DOD; and, to simplify the interface for industry regardless of which military service awarded the contract. However, the Secretary of Defense may permit a military department to be assigned plant cognizance because of specialized supplies and support requirements. The Navy has fourteen Naval Plant Representative Offices (NAVPRO's), sixteen Supervisor of Shipbuilding

Conversion and Repair (SUPSHIP's) and ten other commands with contract administration responsibilities; the Air Force has 26 Air Force Plant Representative Offices (AFPRO's) and fifteen other detachments and offices; the Army has three Army Plant Representative Offices (ARPRO's) and six other commands administering contracts.

Under the DLA's nine DCAS regions (DCASR's) there are 37 DCAS Management Areas (DCASMA's) and 40 DCAS Plant Representative Offices (DCASPRO's). The DCASMA's administer defense contracts with many smaller contractors within a defined area whereas the DCASPRO's work with large contracts performed by one large contractor. The general guidelines for plant cognizance are that a plant will only be assigned to a military department when the department has a contract in the plant for a major system or major subsystem, and that system is of such a critical importance that the performance of contract administration requires unusually close technical direction and control by the appropriate program manager .

The scope of DCAS functions has grown over the years as defense systems become more complex. Newly emerging legal and social issues have also added to this complexity. Perhaps at one end of the spectrum is the simple fixed-price contract for a standard commercial item, where delivery is made from stock and where inspection and acceptance is done completely by the receiving activity. This arrangement requires the least DCAS involvement. At the other end of the spectrum is the cost-plus-award-fee contract for the construction of a new type of ship or aircraft. The DCAS must exercise a wide range of functions for this contract procedure including production interface, cost analysis, issue authorization, repair costs, repair authorization, etc.. [Ref. 11: pp. 69, 81]

To assist with contracting difficulties, the DCAS may call upon the services of the Defense Contract Auditing Agency (DCAA) which operates under the direction of the Office of the Assistant Secretary of Defense (Comptroller). Often a DCAA office will be co-located with the DCAS to facilitate interaction. [Ref. 11: p. 83]

At times, a divergence of contractual interpretation between contracting officer and supplier will lead to disputes. Although the contracting officer has wide powers to resolve differences under contract clauses covering such particulars as engineering changes, Government furnished property, inspections, reimbursement for extra work, etc., the contractor can appeal the contracting officer's final determination to the Armed Services Board of Contract Appeals which derives its jurisdiction from the Contract Disputes Act of 1978, Public Law 95-563, 41 U.S. Congress, 601-613. [Ref. 11: pp. 86 - 87]

4. Summary

Policy development and the four phases of the acquisition process are portrayed above in very simplistic terms. The systems and procedures used to manage risk, budgeting, research, production, deployment, testing and all the myriad of other concerns in the program are very highly developed and complex, requiring considerable study to fully comprehend. The introduction of Government furnishings into this program serves to make the process even more complicated. The contract administration service activities play a large role in helping the DOD to manage the huge, complex acquisition programs of the services.

The next section will examine the reasons for including GFP in the acquisition strategy. For a more detailed presentation of the acquisition

process in the Department of Defense, the Defense Systems Management College has published an excellent text on the subject. [Ref. 21: all]

B. ACQUISITION STRATEGY AND THE USE OF GFP

Department of Defense Directive 5000.1 requires that in the interest of achieving stability, DOD components shall develop an acquisition strategy for each major acquisition. [Ref. 23: p. 2] This strategy is to delineate the objectives, resources, management assumptions, extent of competition, proposed contract types, and program structure and then, tailor them to the prescribed steps in the major system acquisition decision-making process.

In structuring the acquisition strategy, the conceptual basis may be categorized into three essential areas of concern:

- Strategic
- Technical
- Resource [Ref. 21: p. 3-2]

Addressing each of these areas reveals that GFP is an issue that pervades all three and, therefore, should be included as an element critical to the success of the program.

1. Strategic Concerns

The primary elements of strategic concern are as follows:

- National objectives
- Nature of the threat and the technology base
- Program objectives, constraints and priorities
- Market factors
- Critical program issues [Ref. 21: p. 3-5]

In particular, GFP becomes an issue of strategic concern in the area of market factors. Such factors include consideration of:

- Industrial base
- Qualified suppliers
- Competition for scarce resources
- Coproduction overseas

When the Government goes to suppliers, other than the prime contractor, to buy components and subsystems that will be integrated into the end-product, those components and subsystems become GFP as prescribed in the acquisition contract. This activity can have a profound impact upon the industrial base for defense systems production. In breaking out selected components, the Government can involve a larger number of perhaps smaller companies in the defense acquisition process. On the other hand, breaking away certain subsystems from the prime contractor can lower profit margins which may reduce the capability or incentive to build the facilities necessary to provide support in national emergencies.

Also, production overseas may obviate the access to commercial facilities and materials normally available to a domestically located contractor. Consequently, Government furnishings may be the only feasible solution to providing all the necessary resources.

The issue of ensuring the qualifications of suppliers of equipment and materials which are purchased as GFP is, of course, of critical importance, for defective GFP can be very costly and time consuming to the acquisition program.

2. Technical Concerns

Four primary elements comprise the technical concerns:

- Design
- Test and Evaluation
- Production
- Deployment [Ref. 21: p. 3-5]

In selecting GFE or GFM, a careful analysis of design factors must be made. In addition to basic cost and performance criteria, consideration must be given to durability, reliability/maintainability, corrosion resistance, safety/health, human factors, nuclear hardening and functional interface, to name some. GFE and GFM also must meet standardization requirements and carry acceptable warranties or guarantees regarding quality of design. If the GFE/GFM is to be successfully integrated into the system prior to deployment, then test and evaluation procedures must include the anticipated furnished subsystems during prototyping and the qualification, demonstration and acceptance testing that occurs prior to initial production. The timing of GFE/GFM can greatly impact concurrency and sequence of testing while design and production activities are in progress and, therefore, becomes a critical aspect of testing strategy.

Once the systems have been deployed with the furnished components integrated into the end-product, technical concerns regarding installation, supportability, and system growth occur. Areas likely to be affected by the use of Government furnishings in the deployment of major systems are maintenance, training, publications and supporting data, contractor support, facilities and pre-planned product improvement. It is sometimes difficult to avoid the use of GFP and the attendant complexity in

integration and deployment simply because of the sensitive nature of the systems being introduced.

3. Resource Concerns

The predominant interests in resources are represented by the following five elements:

- Personnel/organization
- Schedule
- Business/financial
- Management information
- Facilities

[Ref. 21: pp. 3-7 to 3-9]

Government furnishings have potential for impact upon all of these areas. The integration of GFE requires close coordination of both contractor and Government organizations. Outside organizations such as OMB, GAO, Congress and the news media have had profound effect upon how resources are to be allocated.

From a scheduling view, the critical effects of sequence and timing have already been mentioned. Pacing, duration and the concurrency of activities are contingent upon the issue of GFE/GFM and its condition.

Financial strategy is of major importance to the employment of GFP. Competition is a key element of this strategy along with source selection and the type of contract, incentives and warranties. Once the decision has been made to break out components not already in supply systems, the competing process must be accomplished for these components and appropriate contractual agreements formed. The single most important, overriding criterion for this action is the prospect of substantial cost savings.

Due to the huge quantities of GFP in use, property administrators are increasingly turning to computerized information systems just to be able to keep track of government property. These automated management information systems can take into account schedule control, cost control, interface and configuration control. Networked data base facilities assist various programs in coordinating the allocation and standardization of resources among each other and in effecting proper disposition of excess material and equipment.

The use of Government facilities, equipment and laboratories is an issue which arises in almost every major acquisition program. Needs for modernization or the introduction of new technology can either obviate the use of potential GFP or make its use essential depending upon the situation. Some participants in the DD-963 class destroyer program attribute the program's success to the conscious strategy of minimizing the use of GFE; other programs, such as the F-5E International Fighter, realized the full benefits of extensive use of GFE. [Ref. 21: p. 5-36]

C. SUMMARY

This section was a brief overview of how GFP, in its various forms, constitutes a very important part of acquisition strategy. Some of the many considerations involved in the planning and integration of GFP usage were presented as a basis for assessing how effective management and accounting of GFP should be accomplished.

IV. PROPERTY CONTROL

Each contractor is required to control, protect, preserve and maintain all Government property in possession. The contractor's policies and procedures must clearly delineate the responsibilities for controlling each classification of Government property and provide authority to carry out those responsibilities. The contractor's property control systems should provide for communications between operational divisions and top management personnel; and, the systems should provide for monitoring compliance with documented policies and procedures.

Property Survey Preamble

A. THE PROPERTY ADMINISTRATOR

The preamble to the DCASR Government property survey (above) describes in broad terms the responsibilities of the contractor regarding property furnished by the Government. However, it is the Government's Property Administrators (PA's) who must ensure that the contractors are meeting those responsibilities. Among the general duties of the PA are the following:

- Provide guidance to the contractor in developing and documenting effective procedures for managing GFP.
- Periodically review and approve the contractor's GFP control procedures.
- Develop an annual property administration strategy for each active contractor.
- Insure the availability of records required by the contract and acquisition regulations to present documented evidence regarding transactions involving GFP.

- Periodically conduct surveys of the contractor's plant and facilities to physically inspect the property accounting system and procedures, shipping/receiving and storage areas.
- Investigate cases of loss, damage or destruction of GFP and submit findings and recommendations to the DCAS Commanding Officer.
- Review, approve and monitor contractors procedures for dispositioning excess GFP.
- Withhold approval from contractors whose procedures do not conform to the requirements of the Federal Acquisition Regulation.

B. PROPERTY CONTROL PROCEDURES

In determining that the contractor's methods are suitable for control of the property specified by the contract, the PA will require the contractor to submit procedures which are as complete as possible. A written, detailed description of the contractor's system, identifying each of the individual positions or components of the contractor's organization having specified functions and authority for property management, is recorded.

Additionally, the procedures should specifically address each of the ten categories of property management and the particular process employed in each case. [Ref. 24: pp. S3:23 - S3:28]

C. PROPERTY CATEGORIES

1. Acquisition

This category of property involves both GFP and contractor acquired property procured as a direct charge to the contracts. This property is generally acquired through either of three methods:

1. Purchase orders,

2. Transfer from contractor owned inventory, and
3. Transfer among contracts.

2. Receiving

This process involves initial verification and documentation of physical presence and condition for both GFP and contractor acquired property. Upon acceptance, the contractor becomes both accountable and responsible for the material and immediately identifies and classifies the receipts in the receiving area.

3. Records

This category consists of the official accounting records maintained by the contractor to show status and control over all Government property furnished to or acquired by the contractor.

There are six functional areas within the record category:

1. Inventory control (real and personal property).
2. Fabrication records.
3. Receipt and issue file.
4. Custodial records.
5. Scrap and salvage records.
6. Multicontract cost and material control system.

4. Storage and Movement

The process of warehousing to safely store, protect and preserve GFP and the care in moving GFP while in possession are the purposes of this category.

5. Consumption

Conservation and effectiveness in the consumption of GFP used to accomplish a contract are closely monitored. Excesses are to be promptly returned and actual quantities consumed are compared to planned consumption. Normally a first in, first out (FIFO) system is used for perishable or "dated" inventory.

6. Utilization

Plant equipment, special tooling and special test equipment must be used for the specific purpose intended. Material may not be diverted to other uses without specific written approval from the Contracting Officer.

7. Maintenance

The quality and timeliness of preventative and corrective maintenance are most important to the lengthening of the useful life of Government property. Rehabilitation and major repair work are monitored, reported and analyzed.

8. Physical Inventories

The action of physically locating and counting GFP inventories must be reported, along with a detailed description of adjustments, to the PA. The functional areas of this category are thus: performance, recording and adjustments.

9. Subcontract Control

A prime contractor is expected to exercise the same controls over a subcontractor with respect to Government property. Adequate documentation showing effective prime contractor surveillance over GFP must be filed with and approved by the PA. The subcontractor's property control system will be evaluated in the same manner as that of the prime.

10. Disposition

The contractor must declare unused inventory immediately so that it may be screened against other contracts and needs. The declaration must be complete and accurate; and, proper authorization must be obtained prior to disposition. Proper disposal procedures must be exercised, with related documentation reflecting authority, action taken, and dates; and, a permanent file of these records must be maintained.

D. INITIATION OF PROPERTY ADMINISTRATION

Usually the PA first makes contact with the contractor at the post-award orientation conference at which time a discussion is held regarding property administration problems and responsibilities. The contractor's representatives are designated and the policies, instructions and company procedures for property administration are reviewed. If necessary, the PA will provide guidance to the contractor's representatives.

Next the PA will prepare and file a Property Summary Data Record which contains legal names and addresses, type of contract, date of final review, supporting property administration agreements, and names of company property administrators. [Ref. 24: p. S3:3]

The summary data record is then placed into a Contract Property Control Data File which also includes a copy of the contract; record of initial review, evaluation and approval; record of visits, system surveys performed and work papers; contractor's receipts for Government property; record of final review and closure of contract property account; all pertinent correspondence; records of inspections and audits performed by other agencies; and, contractor prepared reports. [Ref. 24: pp. S3:3 - S3:4]

If the PA finds that the contractor's property control system does not adequately meet the contract requirements, the summary data record is annotated and the contractor is notified in writing of the required corrections. If compliance is not obtained within a reasonable amount of time, the PA must advise the contracting officer of the problem, the contractor's position and the recommended action. The contracting officer may then choose to withhold payments or suspend the contract.

When the contractor's control system is acceptable, the property administrator advises the contractor and the contracting officer by means of a letter of approval. [Ref. 24: pp. S3:5 - S3:7]

E. PLANNING AND COORDINATION

Before any system surveys are conducted, the PA establishes a survey plan that includes: a statement about the current status of the contractor's control procedures; the categories, quantities and location of property; the responsible personnel and their duties; and, work sheets prepared for each category of property along with the statistical sampling techniques to be used. At the beginning of each fiscal year, the PA prepares a schedule of surveys for the entire year. [Ref. 24: p. S3:8]

F. TECHNICAL SUPPORT

In evaluating property control systems, the PA is authorized access to the technical functions of the DCAS organization. Usually pertinent parts of the contract will be referred to the appropriate technical functions for comment or evaluation. In performing surveys, the specialists from these technical functions will, when necessary, assist the PA with inspections. Also, assistance and advice on matters involving analyses of the contractor's books and accounting records and on any other audit issue considered appropriate, must be obtained from the local DCAA auditor. [Ref. 24: p. S3:2]

Table IV-1 outlines the various resources normally available to the PA:

| <u>TECHNICAL AREA</u> | <u>FUNCTIONAL ELEMENT</u> |
|--|----------------------------------|
| Pricing, Financial Statements | Defense Contract Audit Agency |
| Maintenance | Quality Assurance |
| Hazardous Materials Storage | Safety |
| Specifications, Blueprints | Engineering |
| Destruction, Damage Incident to Shipping | Material Control/Quality Control |
| Property Disposition | Plant Clearance Officer |
| Computer Systems | Engineering/Management Support |

**TABLE IV-1: TECHNICAL RESOURCES
AVAILABLE TO THE PROPERTY ADMINISTRATOR**

G. USE OF STATISTICAL SAMPLING

A 90% confidence level is required for sampling of Government property. The PA uses a table of sample sizes from the FAR. This table gives sample

sizes which are calculated to ensure a 90% confidence level that lots having 10% or more defects will be rejected. The test samples are selected using a table of random numbers which are also provided in the supplement.

[Ref. 24: p. S3:13)

H. PERFORMING THE SURVEY

Selection of sample property is made from those units involved in current operations, i.e. 90 days prior or as recent as possible. Units with similar characteristics are combined into single lots and sampled for their common characteristics. Dissimilar characteristics are sampled separately.

After testing is performed, the results are recorded and the findings are analyzed. Conclusions and recommendations are also recorded. Each lot tested is judged as either satisfactory or unsatisfactory.

If any sample is found unsatisfactory during the survey, the PA determines the effects of the defects upon the entire system and all other categories are examined for similar type defects.

At the conclusion of the survey, a formal report is prepared by the PA and sent to the contractor for response. The PA then maintains the results in the Survey Case File to facilitate follow-up of corrective actions.

V. FINDINGS

A. INTRODUCTION

1. Description of Sample

To provide the research background for this study, seven different contract administration offices within the Los Angeles Defense Contract Administration Region (DCASR) were visited: SUPSHIP Long Beach; SUPSHIP San Diego; AFPRO TRW, Redondo Beach; AFPRO Douglas Aircraft Co., Long Beach; ARPRO Hughes Helicopter, Inc., Culver City; and, DCASPRO McDonnell Douglas Astronautics Co., Huntington Beach.

Although this sample size is small compared to the total number of contract administration offices (approximately 177) in the Department of Defense, the sample is considered large enough to provide reliable answers to the research questions and to fulfill the objectives of the study. Since the DOD acquisition program is intended to be standardized across all of the Services and DOD agencies, the sample is quite representative in that at least one example from each of the three Services and the DLA is presented.

2. Assumptions

Central to this study is the assumption that the people who are actually working with a system are those who are best able to judge it. Questions are designed to produce thoughtful responses concerning the system for managing and accounting for GFP and to address the issues which have so troubled our Congressional leaders over the years. Those issues have centered on the adequacy of the system, its structure and the people who operate it. [Ref. 34: p. 16]

3. Interview Procedure

Interviews were conducted with Property Administrators on an informal basis and lasted from 2 to 4 hours in each case. The primary thrust of the questioning was to obtain data which would serve to support an assessment of the adequacy of the DOD GFP management system. Although personnel interviewed were encouraged to offer any information they felt pertinent, answers to four primary questions were sought:

1. Does the FAR create a system that can effectively manage and account for GFP?
2. What changes do you think need to be made to the FAR/DFARS to make them more effective?
3. Is the DCAS (or SUPSHIP, ARPRO, AFPRO, etc.) organization properly structured to effectively manage the GFP now in the system?
4. Is the DCAS (or SUPSHIP, ARPRO, AFPRO, etc.) organization properly staffed to provide the needed control over GFP?

Of course an obvious follow-on question to each of these is: Why? The answers to these questions are summarized in Table V-1 and a more lengthy description of observations from each site is given below.

B. CASE PRESENTATIONS

1. SUPSHIP Long Beach

SUPSHIP Long Beach is located in a modern, three story building at Navy Shipyard Long Beach. The Command of about 150 personnel is headed by a Navy Captain. There are four operational departments: Planning, Contracts, Quality Assurance, and Material. The Property Management Division falls under the Material Department.

The Property Management Offices are located some five miles away from the home office in a trailer situated within the heart of Todd Shipyards. The office is staffed by five people, however, the organizational manning document calls for seven. The Property Management Supervisor is a GS-12, with the other PA's at GS-5 or GS-7 levels. The Supervisor is also assigned collateral duties as Plant Clearance Officer and is the Deputy Material Department Officer. In addition, one of his subordinates is responsible for managing the Buy Our Spares Smart (BOSS) Program -- a job essentially unrelated to the property management function.

The work presently being done involves four long term new construction contracts, three long term leased facilities contracts and eight "semi-permanent" Master Ship Repair contracts. GFM and CFM constitute the predominant types of property employed. The PA Supervisor estimates that SUPSHIP Long Beach is, "number one in property." [Ref. 25]

a. Answers to the research questions.

(1) The Property Management Supervisor stated that the regulations governing property administration were very adequate to accomplish proper control.

(2) One area of the FAR which was felt to be in need of change involved the Government's responsibility to prove "willful misconduct" or "lack of good faith" in the case of mismanagement of GFP in order for the Government to recover losses from the contractor. Proof of willful misconduct in mismanagement cases is very difficult or impossible in civil courts, said the Property Management Supervisor. Removal of the requirement in the FAR to show "willful misconduct" or "lack of good faith" was recommended. [Ref. 24: p. S3:17]

(3) Regarding organizational structure, the Supervisor felt strongly that the Property Management Division should not be under the Material Department. Property Administration, he contended was of such large magnitude and so critically important to the success of the contract that the PA should report directly to the Commander of SUPSHIP.

In addition, the PA function should have the authority to make inputs and give approval in the contract preparation process, since many GFP problems were thought to result from poorly written contracts where GFP is involved. Unfortunately, he explained, the present size of the Property Management Division was not large enough to constitute a full department and, therefore, GS-13 leadership was not possible under Government Service guidelines. He recommended bringing the related QA functions into the Property Management function to help achieve the necessary size.

(4) The staffing of the division was considered a serious problem. The people assigned were judged quite good but simply lacking in experience. Apparently experienced property management personnel have been difficult to retain because they are very quickly hired by commercial companies offering substantially better pay to trained property managers with DCAS backgrounds. Two more people were said to be needed for a total of seven.

2. SUPSHIP San Diego

The San Diego Property Management Division is located in an office building only a short distance from the SUPSHIP Command building. Only three people are assigned to the division which controls property for nine different contractors. One of the PA's (GS-11) works exclusively with NASCO

Shipyards and a second PA (GS-11) handles all other smaller contractors. A third, new PA (GS-9) is being trained to help out with the smaller contracts. Additionally, there are eight expeditors available to work with the PA's to ensure the delivery of material, should they be needed. There is no divisional supervisor for the Property Management workcenter.

A unique feature of the San Diego Command is that it is co-located with a Naval Supply Center. Consequently, contractor inventories were almost nil. The PA's work directly with the contractor's production personnel to arrange for immediate delivery of property when the crews were ready for it, often they personally made deliveries or supervised the conveyance of property. And, again, they were responsible for the plant clearance functions. [Ref. 26]

a. Answers to the research questions.

(1) Generally, the Property Management Specialists were satisfied with the acquisition regulations, however, they had some suggestions.

(2) The consensus among the PA's was that prices of material at the production level did not need to be known for effective property management. As long as original source documents were maintained at the Systems Command, issue and inventory forms should not have to reflect prices. Apparently, Naval Sea Systems Command (NAVSEA) is still not providing unit prices for GFM issues in spite of being ordered to do so nearly a year ago. [Ref. 2: p. 45.505-1] and [Ref. 33: p. 2]

Also, it was felt that commingling of Government property and contractor supplies was sometimes justified and should be allowed, when appropriate.

Mention was made of the lack of reference in the FAR to agencies specifically tasked to handle divestiture of salvage and excess material for other Governmental agencies. These references were considered important since the process can become very complicated and time consuming.

Lastly, the requirement to show "willful misconduct" in the abusive actions of a miscreant contractor was thought to remove any real deterrent the PA's might have to discourage the practice. This criteria should be removed from the FAR, said the PA's.

(3) Due to the tremendous amount of GFM involved in the work at San Diego, the PA's felt that the Property Management Division should properly come under the Material Department, as was the case. The situation outside the SUPSHIP command, however, was viewed with some consternation. The observation was made that there is virtually no one at NAVSEA with property administration experience and knowledge. Often contracts were written with little regard for property management problems. Moreover, it appeared that PA's in the field had no input at all into the contract preparation process. It was noted that cost-reimbursement contracts are "ten times more difficult" to management than fixed-price contracts. It was noted that "almost universally," contracting officers have demonstrated a costly lack of understanding concerning property management.

(4) Regarding the staffing of their workcenter, agreement was unanimous that they were under-staffed. Although the two experienced PA's felt that they were able to control contracted GFM, they acknowledged the unique convenience of having the Supply Center within immediate

access. Also mentioned was the need to have people under training at all times because of the imbalance between commercial and Government pay scales and the high attrition rate among good PA's. At least four PA's were considered necessary for proper management of the contracts currently open, i.e., one additional PA needed.

3. AFPRO DOUGLAS AIRCRAFT COMPANY, LONG BEACH

The AFPRO Command, commanded by an Air Force Colonel, is located inside the Douglas Aircraft Plant in Long Beach. Office facilities are excellent for the approximate 81 persons assigned.

The Industrial Property Branch has been recently shifted from the Manufacturing Operations Division to the Contract Administration Division. There are two Property Management Specialists assigned to the branch: the supervisor (GS-12) and a Property Administrative Assistant (GS-11). In addition, the Plant Clearance Officer (GS-11) as well as a clerk (GS-5) are assigned to the branch.

At this location, the author had the opportunity to visit the contractor's property management workcenter and interview the PA's civilian counterpart. Interestingly, Douglas' key Government property manager had been a PA for the Navy for 31 years prior to taking her present position at Douglas Aircraft.

The property management function at Douglas Aircraft is automated completely and the Government PA's may access the system via a "read-only" monitor. Two programs are used to effect entry: GFE Record Status Report and GFE Material Location Report. The print-outs contain part

numbers, description, customer (USAF or USN), contract, model, serial number, location, unit price, quantity and active date.

Another unique resource used by Douglas Aircraft was a set of "Control Procedures" issued by the Company Vice President (Controller) specifically for "Government Furnished Property Management." [Ref. 27]

a. Answers to the research questions.

(1) Federal Regulations concerning property management were considered inadequate for the reasons stated in (2) below.

(2) The only way to effectively assure proper care and control of Government property, it was said, is for the Government to take the GFP management function away from the contractor and manage the program internally. As long as the contractor controls the official records and maintains the access to inventories, there will always be mismanagement and abuse of the Government's program of furnishing material and equipment. It was noted that in most cases, a major systems contractor has little or no incentive for using GFE; and, often it is to the contractor's disadvantage to manage and account for a component which is in direct competition with the contractor's own products.

The annual requirement for survey of each property area was found to be impossible to accomplish. A two year cycle under present staffing was recommended.

A problem often encountered involved the tendency of contractors to promote company property managers into other divisions after they become experienced. Thus, the Government PA's were usually required to deal with new or inexperienced counterparts. The FAR should

provide for minimum qualifications in the case of contractor staffing for Government property management.

Additionally, the deletion of the FAR requirement to show "willful misconduct" in cases of contractor mismanagement was recommended.

(3) The property management function should be organized as a separate division with a Division Chief at the GM-14 level. The reasons for this structure involved (a) providing the property management function with enough leverage to have a direct input to the Commander and the contracting process and (b) providing a pay incentive to retain qualified people in PA positions.

(4) The Property Branch was said to be quite under-staffed. It was estimated that at least two additional PA's were required to maintain the necessary depth to effectively monitor a contractor as large as this one. Again, the apparent pay imbalance was cited as the primary contributing cause to a high attrition rate. [Ref. 28]

4. AFPRO TRW, Redondo Beach

The primary difference between the Redondo Beach and the Long Beach AFPRO's was that the Redondo Beach Chief Property Management Specialist was operating quite independently of any Divisional Chief. The Property Chief, in fact, has her own division with a staff of four which does get involved with contract design. Another significant difference was that she was about to be promoted to GS-13 -- a level that, it was noted, is more competitive with civilian pay scales.

The property management system at TRW is fully automated (SIMSUP) and processes all GFE/GFM. They anticipate soon implementing

use of portable, hand-held optical character reading (OCR) devices for conducting inventory reviews. The contractor presently employs 14 to 15 people in the property management workcenter.

a. Answers to the research questions.

(1) The FAR procedures were thought to be quite adequate for the property management function.

(2) A two year survey cycle for property areas was considered more reasonable rather than the annual requirement.

(3) The current structure which placed the PA function as a separate division from all others was felt to be the preferred method.

(4) Present staffing was thought to be seriously inadequate after two recent cut-backs. Two additional PA's were felt necessary to properly manage the GFP function at TRW. Again cited was the pay imbalance between Government property management specialists and civilian property managers in attracting and retaining qualified PA's in Government Service.
[Ref. 29]

5. DCASPRO McDonnell Douglas, Huntington Beach

The DCASPRO at Huntington Beach is located within the McDonnell Douglas plant and is commanded by an Army Colonel.

The property management branch fell under the organization of the Contracts Division. The branch was staffed by two PA's with the Chief PA holding a GS-12 position. However, the Property Chief has recently retired, leaving just the one GS-11 PA (who was formerly employed at SUPSHIP Long Beach).

The contractor's property management system was fully automated and used the same control procedures as the Douglas Aircraft facility. There are 17 positions in the contractor's property management workcenter.

a. Answers to the research questions.

(1) The FAR was thought to adequately fulfill the requirements for effective property management support.

(2) The requirement for an annual survey of each property area was considered impossible with present manning. Surveys are presently being accomplished on a two-year cycle and this is felt to be a more reasonable requirement.

The FAR was felt to be much too lenient in deterring abusive use of GFP. The need to prove "willful misconduct" was said to be excessive in cases of loss or damage to GFP.

(3) The need to place the property management function apart from the influence of other divisions was expressed. Ideally, the Property Chief was seen as the head of his own division.

(4) Understaffing was seen as an ongoing problem resulting from the low pay levels at which property management trainees enter the Service and the demand for experienced property specialists in civilian occupations. An additional three people (total of four) were considered necessary to adequately staff the PA function and provide for the property clearance at this DCASPRO.

6. ARPRO Hughes Helicopter's Incorporated, Culver City

The Hughes company is presently in the process of moving most of their operations to Mesa Arizona. Consequently, the ARPRO is also splitting its staffs between the two sites.

The Property Management function is combined with the Production Branch, which is under the Procurement and Production Division, and consists of two PA's (GS-12 and 11) and three Industrial Support Specialists (GS-12/11). Because of the two locations, only one PA is available at each site.

The contractor's property management system is automated and may be accessed by a "Daily Asset Report" which is quite detailed and lists unit prices of all GFE/GFM. [Ref. 30]

a. Answers to to the research questions.

(1) The FAR coverage of the property management function was thought to be adequately developed.

(2) The property management specialist at this contractor site felt that there was little that could be done at the PA level to obtain contractor compliance with regulations. While he could make no specific recommendations, he felt that the FAR should be written to give the PA function a means of directly obtaining contractor compliance.

(3) Under the ARPRO's existing structure, the PA function was not clearly distinguishable as an organizational entity. As a small part of the Production/Industrial Branch, the PA's were required to request assistance from the Quality Assurance Division for the accomplishment of their property surveys. It was felt that more autonomy from other functional

areas would provide more visibility and leverage to accomplish the control of the GFE and GFM in the contractor's possession.

(4) With the ARPRO staff being divided between two widely separated geographic locations, the perceived lack of adequate staffing was greatly exacerbated. The feeling was that the situation might improve once the transition to the new location was complete. Meanwhile the tasks of approving new storage facilities, breaking-in new people at the new location, monitoring the movement of huge existing inventories, etc., have apparently overwhelmed the PA's.

7. DCASMA San Diego

The San Diego DCAS Management Area Office, commanded by a Navy Captain, consisted of approximately 125 people of which twelve were assigned to the Property Group.

A significant difference between the DCASMA and the other contract administration offices visited is that rather than dealing with only one contractor, the DCASMA handles many contracts done by smaller companies. The typical case-load for the PA was from 40 to 60 contracts.

Although use of automated systems was encouraged, contractors at this scale seldom computerize their property management systems. [Ref. 31]

a. Answers to the research questions.

(1) The provision in the FAR which allows the contractor to control and manage the official records for and take custody of Government property is viewed as a key weakness in the system. It was felt that, in general, contractors do not take the GFP program very seriously and seem to believe that expedience in the execution will always take precedence over the manner in which they manage property furnished by the Government.

Often the production requirements of the services speed the contractor well into the job before the complex requirements of GFP control can be implemented and formally approved.

(2) To give teeth to the PA function, the Property Group Manager should have the power to suspend work on the contract, it was said. Often, the designated contracting officer has little understanding of the implications involved in property management and its potential costs to the Government in cases of mismanagement.

The requirement to show "willful misconduct" or "lack of good faith" in recovering losses from contractors was identified as a major flaw in the FAR.

Additionally, the FAR should require that contractor personnel in property management positions must attain basic minimum training and proficiency qualifications. Presently, DCASMA Property Management Specialists are spending an inordinate amount of time in providing guidance and training to the contractor's employees. This activity detracted their attention from other contracts and provided an expensive service to the contractor free of charge.

(3) The scope of the activities of the Contract Property Management Group was felt to be of sufficient magnitude to constitute designation as a division rather than as a group. The function should then be placed on a level equal to the Contract Management Division rather than in a subordinated role. The role of Property Management could then be expanded to include contract design for property control and power to withdraw contracts due to mismanagement of property control systems. The contracting officers at DCAS were not considered knowledgeable enough

concerning property management to properly design contracts involving Government furnished property.

(4) Case load for PA's was considered quite excessive at 40 contracts per PA. Three additional property management specialists were needed to cover the San Diego area.

C. SUMMARY

All of the PA's interviewed were surprisingly candid about their role in contract administration and their position in the organization. With only one exception, AFPRO TRW, the PA's felt that they were somewhat excluded from the "team" when it came to contract design. This often led to poorly drawn contracts with regard to the property management function. For example, cost reimbursement contracts involving GFE were said to be much more costly and difficult to administer than a fixed cost contract. The PA's felt that considerations such as these were apparently not made in many cases and resulted in unnecessary expense to the Government.

An additional observation was that many feel somewhat powerless to strictly enforce the FAR requirements. First, the contractor is usually quite reluctant to invest in the manning and facilities necessary to properly handle Government property. Since contractors are profit motivated, this is quite natural.

Secondly, the PA's only recourse is to report an unsatisfactory system to the contracting officer and make recommendations -- the PA cannot take direct action. However, the contracting officer, who very often has no training in property management, is frequently inclined to accommodate the contractor in order to speed production.

Thirdly, there is very little a contracting officer can do in the way of taking action against the contractor for alleged abuses. If the contractor forces the issue into civil courts, the problem of substantiating "willful misconduct" in cases of loss or damage to GFP is nearly insurmountable.

A fourth difficulty is that there are simply not enough Government property managers to adequately survey the huge inventories of GFP. The use of automated systems was seen as a possible solution to this problem, however, automation also brings the added task of auditing the computer software used to accomplish property control. This activity requires a person with exceptional skills in programming, and those people are not currently available to DCAS organizations and are extremely well-paid in commercial practice.

At each organization visited, the author found the Property Management Specialists to be exceptionally cooperative and helpful in answering questions and providing information about their unique operations. The sentiment expressed among virtually all the people interviewed was that Congressional hearings and unfavorable news media coverage had severely distorted and misrepresented actual conditions in industry and had brought unfair criticism to their profession. It was almost as if many perceived the inquiry as an opportunity to tell their side of the story. Each individual who participated in the interviews, without exception, made a pointed effort to emphasize the importance of their work and the challenges involved in getting the job done correctly.

**TABLE V-1
SUMMARY OF FINDINGS**

| <u>SITE</u> | <u>ADEQUATE SYSTEM</u> | <u>RECOMMENDED CHANGES</u> | <u>ADEQUATE STRUCTURE</u> | <u>ADEQUATE STAFFING</u> |
|---|----------------------------|--|---|------------------------------|
| SUPSHIP San Diego | Yes | - Delete "willful misconduct" - Unit prices not needed | SUPSHIP OK NAVSEA needs PA function | One more pers needed |
| SUPSHIP Long Beach | Yes | - Delete "willful misconduct" clause | PA function should be a Division w/GS13 | need two more pers |
| AFPRO DAC Long Beach | No | - KTR should not control GFP - Two year cycle - Min quals for KTR Prop Mgrs - Delete "willful misconduct" clause | PA function should be a Division w/GM 14 | need two more pers |
| AFPRO TRW Redondo Beach | Yes | - Two year survey cycle - Delete "willful misconduct clause | PA function is a Division w/GS 13 | need two more pers |
| DCASPRO McDonnell Douglas, Huntington Beach | No | - Delete "willful misconduct" - Two year survey cycle | PA function should be a Division w/GS13 | need three more pers |

LEGEND:

KTR - CONTRACTOR

PA - PROPERTY ADMINISTRATOR

(continued on page 62)

| <u>SITE</u> | | <u>RECOMMENDED CHANGES</u> | <u>ADEQUATE STRUCTURE</u> | <u>ADEQUATE STAFFING</u> |
|---|-----|---|--|------------------------------|
| ARPRO Hughes Helicopter, Culver City | Yes | - PA authority to approve contract | More autonomy for PA function | need two more pers |
| DCASMA San Diego | No | - KTR should not control GFP - PA have contract authority - Delete "willful misconduct clause - Min quals for KTR Prop Mgmt pers | PA function should be a Division | need three more pers |

TABLE V-1
SUMMARY OF FINDINGS
(contd.)

VI. CONCLUSIONS AND RECOMMENDATIONS

A. GENERAL

The four questions posed during the interviews evoked considerable constructive response from the Property Administrators. Their great concern over the highly publicized events of the past six years involving allegations of contractor mismanagement and abusive practices was clearly reflected in their eagerness to talk about problems and possible solutions.

Although the system for managing and accounting for Government furnishings appears to be operating with some success, the answers to the questions leave little doubt that there are still some formidable obstacles yet to be overcome.

B. SPECIFIC CONCLUSIONS

1. System Adequacy

A classic remark was made during the course of one interview which deserves repeating at this point. While reflecting on the provisioning of Government property, one straight-faced PA dryly observed that, "The process is a lot like asking the family dog to guard the meat!"

Certainly this remark was not meant to allude to actual conditions in the industry; however, it does serve to illustrate the problem as seen by at least three of the respondents. The situation becomes somewhat tenuous when an external agency attempts to perform an internal audit function. Essentially, the PA function is much like an internal audit in that compliance with regulations is verified, efficiency and economy are measured and

periodic assessments are made of inventories and record-keeping practices. The difference, in this case, is that the participants have opposing objectives. Government administrators seek to minimize costs and delays while the contractor's goal is to maximize profits.

If the PA is to ensure that Government property is honestly and properly used, he would wish to be able to exercise very close control over that property. Under the FAR, however, the Government gives up not only possession of the property early-on, but also the official record-keeping responsibility. To a cautious property owner, this practice may seem extremely risky. Nevertheless, the fact that the majority of the PA's saw Government and contractor working together for a common cause regarding national defense, indicates that the system does have merit and that a cooperative effort can be successful.

Question (2) is very similar to question (1), but allows the respondent to recommend improvements in addition to making an overall assessment of the system.

2. Recommended Modifications

a. Risk and "Willful Misconduct"

Based upon the observations of the PA's, risk of loss, damage or destruction to Government property in the hands of the contractor is carried almost totally by the Government. This condition occurs because of clauses in the FAR which state that, "the contractor assumes risk for all Government property provided . . . with the exception of loss, damage, or destruction . . . in connection with which there was no willful misconduct or lack of good faith of any of the contractor's managerial personnel" [Ref. 24: S3:17]

The consequence of this wording has been to virtually prohibit the Government from successfully recovering for the value of GFP lost to contractor negligence or mismanagement. PA's universally consider this to be a gross imbalance in favor of the contractor and cite this as a major reason for poor attitudes and lack of concern by contractors in providing sound property management systems.

b. Contract Approval Authority

The recommendation to provide PA's more input for contracts involving Government property is a direct result of the fact that contracting officers receive almost no training for, and usually have little understanding of, the property management function and the related problems and costs involved. If contracting officers begin to make property administration a key part of their training and contracting strategy, this complaint will subside.

c. Two Year Intervals for Surveys

The causes for this suggestion reside in the issue of understaffing. The inability to review all areas on an annual basis logically produces the inclination to change the standard rather than attempting to achieve an impossible objective.

d. Minimum Qualifications for Contractor Personnel

The most perfectly designed systems will not function well if they are not given proper support. The advocacy of setting minimum basic qualifications for training, experience and competency is founded upon the knowledge that, in many cases, mismanagement may result simply from a lack of understanding and proficiency. This problem is especially prevalent among contractors who are initially entering the defense industry. All too

often it is the Government's Property Administrator who must bring the contractor up to standards by personally providing the necessary instruction. The necessity of providing this "service" to the contractor places yet another burden upon the already over-extended PA.

3. Adequacy of Structure

The overwhelming consensus of opinion was that the property management function in all contract administration offices occupies a low level in the organizational structure. Usually the function is organized as a sub-division of a major department. However, in one case (ARPRO Culver City), the PA's were only a part of a branch (or sub-division).

A notable exception to this was the AFPRO TRW, Redondo Beach, which was recently given the status of a separate division with an opportunity for the supervisor to rise to GS 13. Additionally, this AFPRO's PA Chief did have input authority to the contracting process. This situation is evidently peculiar to only the TRW AFPRO and not AFPRO's in general.

The evolution of the PA function into a full divisional structure is a logical expectation, given Congressional and DOD level pressures to upgrade the property administration occupations. Under the Government Service standards for promotion, this divisional authority is a requirement for advancement to GS 13 and GM 14 levels. Presently, the possibility for this progression is not available to the property management specialist. (All PA's interviewed were at the GS 12 level and below.)

With major divisional authority, PA's will have direct lines of communication with the DCAS Commander and will as a likely consequence have much greater influence over the way in which contracts are drawn.

Moreover, with increased opportunity for career advancement in the PA specialty, attrition of top quality administrators is much less likely to occur.

4. Adequacy of Staffing

At each site visited, the impact of critical shortages in trained property management specialists was stressed. From Table V-1, it can be seen that for the seven sites, a total of fifteen additional people were said to be needed. For a total workforce of 30 in the seven PA offices visited, this perceived requirement represents a 50% increase in staffing.

Suggested changes to the system could serve to ameliorate this crisis in staffing. The two-year cycle for surveys, increasing the risks for the contractor, better organization of the PA function, automatic data processing, etc., have all been associated with increasing the PA's ability to administer the use of Government property. However, until those concepts are implemented and are positively contributing to the management process, the obvious shortages in qualified property management specialists will continue to inhibit the most provident application of Government furnished property.

C. RECOMMENDATIONS

1. Shared Risk

The sharing of risk between Government and the contractors is clearly unbalanced. The disproportionate advantages of the contractor have contributed to an unhealthy climate in the management of Government furnished property and should be brought back into balance. Removing the requirement to show "willful misconduct" or "lack of good faith" is a requisite initial step toward equality in the sharing of risk for GFP.

2. Organization

The establishment of the property administration function as a key participant in the contract administration process is essential to the proper management of Government furnishings. The Chief property administrator should have direct input to the organizational commander and the contracting process. The PA function should be organized as a major department in the organization with "sufficient staffing" to support the progression of the PA to GM 14.

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APPENDIX A

EXECUTIVE OFFICE OF THE PRESIDENT
OFFICE OF MANAGEMENT AND BUDGET
WASHINGTON, D.C. 20503

April 5, 1976

CIRCULAR NO. A-109

TO THE HEADS OF EXECUTIVE DEPARTMENTS AND ESTABLISHMENTS

SUBJECT: MAJOR SYSTEM ACQUISITIONS

1. Purpose. This Circular establishes policies, to be followed by executive branch agencies in the acquisition of major systems.
2. Background. The acquisition of major systems by the Federal Government constitutes one of the most crucial and expensive activities performed to meet national needs. Its impact is critical on technology, on the Nation's economic and fiscal policies, and on the accomplishment of Government agency missions in such fields as defense, space, energy and transportation. For a number of years, there has been deep concern over the effectiveness of the management of major system acquisitions. The report of the Commission of Government Procurement recommended basic changes to improve the process of acquiring major systems. This Circular is based on executive branch consideration of the Commission's recommendations.
3. Responsibility. Each agency head has the responsibility to ensure that the provisions of this Circular are followed. This Circular provides administrative direction to heads of agencies and does not establish and shall not be construed to create any substantive or procedural basis for any

person to challenge any agency action or inaction on the basis that such action was not in accordance with this Circular.

4. Coverage. This Circular covers and applies to:

a. Management of the acquisition of major systems, including: -An analysis of agency missions -Determination of mission needs -Setting of program objectives -Determination of system requirements -System program planning -Budgeting -Funding -Research -Engineering -Development -Testing and evaluation -Contracting -Production -Program and management control -Introduction of the system into use or otherwise successful achievement of program objectives.

b. All programs for the acquisition of major systems even though:

(1) The system is one-of-a-kind.

(2) The agency's involvement in the system is limited to the development of demonstration hardware for optional use by the private sector rather than for the agency's own use.

5. Definitions. As used in this Circular:

a. Executive agency (hereinafter referred to as agency) means an executive department, and an independent establishment within the meaning of sections 101 and 104 (1), respectively, of Title 5, United States Code.

b. Agency component means a major organizational subdivision of an agency. For example: The Army, Navy, Air Force, and Defense Supply Agency are agency components of the Department of Defense. The Federal Aviation Administration, Urban Mass Transportation Administration, and

the Federal Highway Administration are agency components of the Department of Transportation.

c. Agency missions means those responsibilities for meeting national needs assigned to a specific agency.

d. Mission need means a required capability within an agency's overall purpose, including cost and schedule considerations.

e. Program objectives means the capability, cost and schedule goals being sought by the system acquisition program in response to a mission need.

f. Program means an organized set of activities directed toward a common purpose, objective, or goal undertaken or proposed by an agency in order to carry out responsibilities assigned to it.

g. System design concept means an idea expressed in terms of general performance, capabilities, and characteristics of hardware and software oriented either to cooperate or to be operated as an integrated whole in meeting a mission need.

h. Major system means that combination of elements that will function together to produce the capabilities required to fulfill a mission need. The elements may include, for example, hardware, equipment, software, construction, or other improvements or real property. Major system acquisition programs are those programs that (1) are directed at and critical to fulfilling an agency mission, (2) entail the allocation of relatively large resources, and (3) warrant special management attention. Additional criteria and relative dollar thresholds for the determination of agency programs to

be considered major systems under the purview of this Circular, may be established at the discretion of the agency head.

i. System acquisition process means the sequence of acquisition activities starting from the agency's reconciliation of its mission needs with its capabilities, priorities and resources, and extending through the introduction of a system into operational use or the otherwise successful achievement of program objectives.

j. Life cycle cost means the sum total of the direct, indirect, recurring, nonrecurring, and other related costs incurred, or estimated to be incurred, in the design, development, production, operation, maintenance and support of a major system over its anticipated useful life span.

6. General policy. The policies of this Circular are designed to assure the effectiveness and efficiency of the process of acquiring major systems. They are based on the general policy that Federal agencies, when acquiring major systems, will:

a. Express needs and program objectives in mission terms and not equipment terms to encourage innovation and competition in creating, exploring, and developing alternative system design concepts.

b. Place emphasis on the initial activities of the system acquisition process to allow competitive exploration of alternative system design concepts in response to mission needs.

c. Communicate with Congress early in the system acquisition process by relating major system acquisition programs to agency mission needs. This communication should follow the requirements of Office of Management

and Budget (OMB) Circular No. A-109 concerning information related to budget estimates and related materials.

d. Establish clear lines of authority, responsibility, and accountability for management of major system acquisition programs. Utilize appropriate managerial levels in decision making, and obtain agency head approval at key decision points in the evolution of each acquisition of each acquisition program.

e. Designate a focal point responsible for integrating and unifying the system acquisition management process and monitoring policy implementation.

f. Rely on private industry in accordance with the policy established by OMB Circular No. A-76.

7. Major system acquisition management objectives. Each agency acquiring major systems should:

a. Ensure that each major system: Fulfills a mission need. Operates effectively in its intended environment. Demonstrates a level of performance and reliability that justifies the allocation of the Nation's limited resources for its acquisition and ownership.

b. Depend on, whenever economically beneficial, competition between similar or differing system design concepts throughout the entire acquisition process.

c. Ensure appropriate trade-off among investment costs, ownership costs, schedules, and performance characteristics.

d. Provide strong checks and balances by ensuring adequate system test and evaluation. Conduct such tests and evaluation independent, where practicable, of developer and user.

e. Accomplish system acquisition planning, built on analysis of agency missions, which implies appropriate resource allocation resulting from clear articulation of agency mission needs.

f. Tailor an acquisition strategy for each program, as soon as the agency decides to solicit alternative system design concepts, that could lead to the acquisition of a new major system and refine the strategy as the program proceeds through the acquisition process. Encompass test and evaluation criteria and business management considerations in the strategy. The strategy could typically include: -Acquisition program -Scheduling of essential elements of the acquisition process -Demonstration, test, and evaluation criteria -Content of solicitations for proposals -Decisions on whom to solicit -Methods for obtaining and sustaining competition or rejection of proposals -Goals for design-to-cost -Methods for projecting life cycle cost -Use of data rights -Use of warranties -Methods for analyzing and developing contractor incentives -Selection of the type of contract best suited for each stage in the acquisition process -Administration of contracts.

g. Maintain a capability to: -Predict, review, assess, negotiate and monitor costs for system development, engineering, design, demonstration, test, production, operation and support (i.e., life system.e costs) -Assess acquisition cost, schedule and performance experience against predictions, and provide such assessments for consideration by the agency head at key decision points -Make new assessments where significant costs, schedule or performance variances occur -Estimate life cycle costs during system design concept evaluation and selection, full-scale development, facility conversion,

and production, to ownership costs, schedules, and performance -Use independent cost estimates, where feasible, for comparison purposes.

8. Management structure.

a. The head of each agency that acquires major systems will designate an acquisition executive to integrate and unify the management process for the agency's major system acquisitions and to monitor implementation of the policies and practices set forth in this Circular.

b. Each agency that acquires -- or is responsible for activities leading to the acquisition of-- Major systems will establish clear lines of authority, responsibility, and accountability for management of its major system acquisition programs.

c. Each agency should preclude management layering and placing nonessential reporting procedures and paperwork requirements on program managers and contractors.

d. A program manager will be designated for each of the agency's major system acquisition programs. This designation should be made when a decision is made to fulfill a mission need by pursuing alternative system design concepts. It is essential that the program manager have an understanding of user needs and constraints, familiarity with development principles, and requisite management skills and experience. Ideally, management skills and experience would include: -Research and development -Operations -Engineering -Construction -Testing -Contracting -Business -Budgeting -Finance. With satisfactory performance, the tenure of the program manager should be long enough to provide continuity and personal accountability.

e. Upon designation, the program manager should be given budget guidance and a written charter of his authority, responsibility, and accountability for accomplishing approved program objectives.

f. Agency technical management and Government laboratories should be considered for participation in agency mission analysis, evaluation of alternative system design concepts, and support of all development, test, and evaluation efforts.

g. Agencies are encouraged to work with each other to foster technology transfer, prevent unwarranted duplication of technological efforts, reduce system costs, promote standardization, and help create and maintain a competitive environment for an acquisition.

9. Key decisions. Technical and program decisions normally will be made at the level of the agency component or operating activity. However, the following four key decision points should be retained and made by the agency head:

a. Identification and definition of a specific mission need to be fulfilled, the relative priority assigned within the agency, and the general magnitude of resources that may be invested.

b. Selection of competitive system design concepts to be advanced to a test/demonstration phase or authorization to proceed with the development of noncompetitive (single concept) system.

c. Commitment of a system to full-scale development and limited production.

d. Commitment of a system to full production.

10. Determination of mission needs.

a. Determination of mission need should be based on an analysis of an agency's mission reconciled with overall capabilities, priorities and resources. When analysis of an agency's mission shows that a need for a new major system exists, such a need should not be defined in equipment terms, but should be defined in terms of the mission, purpose, capability, agency components involved, schedule and cost objectives, and operating constraints. A mission need may result from a deficiency in existing agency in response to a technologically feasible opportunity. Mission needs are independent of any particular system or technological solution.

b. Where an agency has more than one component involved, the agency will assign the roles and responsibilities of each component at the time of the first key decision. The agency may permit two or more agency components to sponsor competitive system design concepts in order to foster innovation and competition.

c. Agencies should, as required to satisfy mission responsibilities, contribute to the technology base, effectively utilizing both the private sector and Government laboratories and in-house technical centers, by conducting, supporting, or sponsoring: -Research -System design concept studies -Proof of concept work -Exploratory subsystem development -Tests and evaluations. Applied technology efforts oriented to system developments should be performed in response to approved mission needs.

11. Alternative systems.

a. Alternative system design concepts will be explored within the context of the agency's mission need and program objectives -- with emphasis on generating innovation and conceptual competition from

industry. Benefits to be derived should be optimized by competitive exploration of alternative system design concepts, and trade-offs of capability, schedule, and cost. Care should be exercised during the initial steps of the acquisition process not to conform mission needs or program objectives to any known systems or products that might foreclose consideration of alternatives.

b. Alternative system design concepts will be solicited from a broad base of qualified firms. In order to achieve the most preferred system solution, emphasis will be placed on innovation and competition. To this end, participation of smaller and newer businesses should be encouraged. Concepts will be primarily solicited from private industry and, when beneficial to the Government, foreign technology and equipment may be considered.

c. Federal laboratories, federally funded research and development centers, educational institutions, and other not-for-profit organizations may also be considered as sources for competitive system design concepts. Ideas, concepts, or technology, developed by Government laboratories or at Government expense, may be made available to private industry through the procurement process or through other established procedures. Industry proposals may be made on the basis of feasible alternatives which the proposer considers superior.

d. Research and development efforts should emphasize early competitive exploration of alternatives, as relatively inexpensive insurance

against premature or preordained choice of a system that may prove to be either more costly or less effective.

e. Requests for alternative system design concept proposals will explain the mission need, schedule, cost, capability objectives, and operating constraints. Each offeror will be free to propose his own technical approach, main design features, subsystems, and alternatives to schedule, cost and capability goals. In the conceptual and less than full-scale development stages, contractors should not be restricted by detailed Government specifications and standards.

f. Selections from competing system design concept proposals will be based on a review by a team of experts, preferably from inside and outside the responsible component development organization. Such a review will consider: (1) Proposed system functional and performance capabilities to meet mission needs and program objectives, including resources required and benefits to be derived by trade-offs, where feasible, among technical performance, acquisition costs, ownership costs, time to develop and procure; and (2) The relevant accomplishment record of competitors.

g. During the uncertain period of identifying and exploring alternative system design concepts, contracts covering relatively short time periods at planned dollar levels will be used. Timely technical reviews of alternative system design concepts will be made to effect the orderly elimination of those least attractive.

h. Contractors should be provided with operational test conditions, mission performance criteria, and life cycle cost factors that will be used by

the agency in the evaluation and selection of the system(s) for full-scale development and production.

i. The participating contractors should be provided with relevant operational and support experience through the program manager, as necessary, in developing performance and other requirements for each alternative system design concept as tests and trade-offs are made.

j. Development of subsystems that are intended to be included in a major system acquisition program will be restricted to less than fully designed hardware (full-scale-development) until the subsystem is identified as a part of a system candidate for full-scale development. Exceptions may be authorized by the agency head if the subsystems are long lead time items that fulfill a recognized generic need or if they have a high potential for common use among several existing or future systems.

12. Demonstrations.

a. Advancement to a competitive test/demonstration phase may be approved when the agency's mission need and program objectives are reaffirmed and when alternative system design concepts are selected.

b. Major system acquisition programs will be structured and resources planned to demonstrate and evaluate competing alternative system design concepts that have been selected. Exceptions may be authorized by the agency head if demonstration is not feasible.

c. Development of a single system design concept that has not been competitively selected should be considered only if justified by factors such as urgency of need, or by the physical and financial impracticality of demonstrating alternatives. Proceeding with the development of a noncompetitive (single concept) system may be authorized by the agency

head. Strong agency program management and technical direction should be used for systems that have been neither competitively selected nor demonstrated.

13. Full-scale development and production.

a. Full-scale development, including limited production, may be approved when the agency's mission need and program objectives are reaffirmed and competitive demonstration results verify that the chosen system design concept(s) is sound.

b. Full production may be approved when the agency's mission need and program objectives are reaffirmed and when system performance has been satisfactorily tested, independent of the agency development and user organizations, and evaluated in an environment that assures demonstration in expected operational conditions. Exceptions to independent testing may be authorized by the agency head under such circumstances as physical or financial impracticability or extreme urgency.

c. Selection of a system(s) and contractor(s) for full-scale development and production is to be made on the basis of (1) system performance measured against current mission need and program objectives, (2) an evaluation of estimated acquisition and ownership costs, and (3) such factors as contractor(s) demonstrated management, financial, and technical capabilities to meet program objectives.

d. The program manager will monitor system tests and contractor progress in fulfilling system performance, cost, and schedule commitments. Significant actual or forecast variances will be brought to the attention of the appropriate management authority for corrective action.

14. Budgeting and financing. Beginning with FY 1979, all agencies will, as part of the budget process, present budgets in terms of agency missions in consonance with Section 201 (i) of the Budget and Accounting Act, 1921, as added by Section 601 of the Congressional Budget Act of 1974, and in accordance with OMB Circular A-11. In so doing, the agencies are desired to separately identify research and development funding for: (1) The general research and development efforts in support of the agency's overall missions, (2) The specific development efforts in support of alternative system design concepts to accomplish each mission need, and (3) Full-scale developments. Each agency should ensure that research and development is not undesirably duplicated across its missions.

15. Information to Congress.

a. Procedures for this purpose will be developed in conjunction with the Office of Management and Budget and the various committees of Congress having oversight responsibility for agency activities. Beginning with FY 1979 budget, each agency will inform Congress in the normal budget process about agency missions, capabilities, deficiencies, and needs and objectives related to acquisition programs in consonance with Section 601 (i) of the Congressional Budget Act of 1974.

b. Disclosure of the basis for an agency decision to proceed with a single system design concept without competitive selection and demonstration will be made to the congressional authorization and appropriation committees.

16. Implementation. All agencies will work closely with the Office of Management and Budget in resolving all implementation problems.

17. Submissions to Office of Management and Budget. Agencies will submit the following to OMB:

- a. Policy directives, regulations, and guidelines as they are issued.
- b. Within six months after the date of this Circular, a time-phased action plan for meeting the requirements of this Circular.
- c. Periodically, the agency approved exceptions system acquisition trends and in monitoring implementations of this policy.

18. Inquires. All questions or inquiries should be submitted to the OMB, Administrator for Federal Procurement Policy. Telephone number, area code, 202-395-4677.

HUGH E. WITT

ADMINISTRATOR FOR FEDERAL PROCUREMENT POLICY

Approved: JAMES T. LYNN

DIRECTOR

APPENDIX B

STATEMENT

BY

MR. JOHN A. MITTINO

DEPUTY ASSISTANT SECRETARY DEFENSE

(PRODUCTION SUPPORT)

BEFORE THE

SUBCOMMITTEE ON LEGISLATION AND NATIONAL SECURITY

COMMITTEE ON GOVERNMENT OPERATIONS

U. S. HOUSE OF REPRESENTATIVES

ON

MARCH 20, 1986

Mr. Chairman and members of the committee, I appreciate this opportunity to appear before you in connection with your continuing interest in Government property. I will relate this subject to broader areas of the industrial base, initiatives to encourage contractor investment in capital equipment, the Secretary's responsibilities under the Defense Industrial Reserve Act of 1973 and our policies to reduce Government ownership of property.

The Department of Defense (DOD) relies on a strong industrial base to produce defense goods for national security. We know that a part of this base is owned by the Government and DOD policies stemming from the Defense Industrial Reserve Act of 1973 is to place maximum reliance upon private industry to provide plant and equipment for defense production. To accomplish this we must obtain increased contractor capital investment.

We are taking direct steps to obtain such investment and also to improve productivity by providing industry with economic incentives to modernize plant and equipment. A major effort in this regard is the Industrial Modernization Incentive Program (IMIP). IMIP is aimed at fostering increased defense contractor capital investment that results in increased productivity, improved quality, reduced DOD acquisition costs, and an enhanced industrial base. The main focus is on encouraging contractors to invest their own funds for this purpose. The primary incentives are shared savings, contractor investment protection, award fees, and others that may be appropriate. IMIP is an acquisition tool with application when specific criteria (investment over and above what would otherwise be made, evidence of cost reductions to the DOD, etc.) are met. It is a targeted and

controlled way of achieving its intended results. Negotiation of a "business agreement" with benefits to both parties is the key to the process.

The IMIP has been in a test phase since November 1982. A policy documentation package (DOD FAR supplement coverage, a DOD directive and a DOD guide) is in the formal coordination process in the near future, will facilitate broader military department implementation and full realization of benefits that are possible.

Before discussing that part of the industrial base that is owned by the Government, I think it is relevant to so how we got into our ownership posture. Most DOD production facilities were established in the World War II era, when sizeable Government investment was required to insure that national defense needs were satisfied. Contractor-owned facilities were augmented during that period to support the war effort. That is why, in come cases, you will find contractor and Government-owned plants sharing common walls, utility systems, etc.. Many of these activities continue to support current, as well as the emergency industrial preparedness base.

Our policy for over 20 years has been to reduce ownership to the minimum essential to support emergency defense requirements. This is generally referred to as the "facilities phase down" policy. To prepare for these hearings, we collected information to assess the impact of Government property on defense production. The information collected, which I will share with you, confirmed my belief that there is no such this as a defense industrial base with the possible exceptions of the ammunition and tank bases. There is a U. S. industrial base of which defense is one of the customers. The data shows:

- Government-owned contractor-operated (GOCO's) plants numbered 112 in FY 69. There are 64 GOCO's today.
- 24 of today's 64 GOCO's are Army ammunition plants. These 24, as well as others, have both peacetime and mobilization requirements.
- In FY 85 we did business with 33,515 contractors that received contracts above \$25,000.
- Approximately 5,000 contractors are in possession of Government property.
- Since 1971, industrial plant equipment (IPE) in the possession of contractors has decreased from \$2.0 to \$1.6 billion. Not dramatic perhaps, but clearly a decrease during a time of growing budgets and inflation. A statistic that is of importance is that of industry's investment. The aerospace industry's annual investment has approximated \$3 billion during each of the past five years. The manufacturing industry has ranged between \$112 and \$138 billion during the same period.

We are aware that other plant equipment (OPE) increased from \$1.9 billion in 1971 to \$4 billion in 1984. Our initial review indicates that a portion (\$1 to \$1.5 billion during FY 84) of the OPE is isolated in non-industrial type locations such as the Defense Early Warning System (DEW Line).

However, we are concerned about the growth in OPE by all three services during the same period when DOD policy emphasis is on contractor investment. Other than a policy change that resulted in some IPE being reclassified as OPE, we have no ready answers for the increases. We do see the need for increased visibility and an improved DOD industrial property management system, that I will discuss later.

When one views the amount of Government-owned property in the possession of contractors from the perspective of our total defense business less than 15 percent of the contractors possess such property. Even though Government-owned property is a relatively minor part of the industrial base, our management efforts have been increasing because we see the need for the military departments and defense logistics agency to be fully accountable for all Government-owned property that is under their administration and control.

In the late 1960's SECDEF recognized the need to establish a formal program to reduce Government ownership of industrial facilities. In 1970, the facilities phase out policy was established to accomplish this reduction. It was later retitled "the phase down policy" in recognition of the fact that facilities required to support certain mobilization requirements (such as ammunition plants) will probably need to be retained.

The phase down policy has been successful to the point that we now own fewer plants and less industrial plant equipment (IPE). Over the years the Air Force has been very active in implementing this policy, particularly the negotiated sale of plants and associated equipment to using contractors. They presently have two other plants with the General Services Administration (GSA) for sale and have identified four other potential candidates. The Navy made a significant divestiture of GOCO plants in the late 50's and early 60's. This type of property reduction will continue. I was recently informed and am pleased to report that the Army and Navy are currently reviewing their GOCO's to determine possible candidates for sale under the authorities of the Federal Property and Administrative Services Act of 1949.

We know we have property in contractor-owned and contractor-operated (COCO) plants that is "excess to ownership" but is required for current production. The Office of the Secretary of Defense (OSD) General Counsel has issued the opinion that there is no clear-cut authority to negotiate a sale of this type of property to using contractors. Without such authority, it is difficult to fully implement the phase down policy. This lack of authority is one reason the phase down policy has not been as successful as we would like. The GAO General Counsel has been investigating this area as well, to determine if in his opinion any authorities do exist to permit such sales. If needed, we have drafted legislation to obtain such sales authority in order to alleviate this constraint to the phase down policy. I should point out, however, that previous legislation of this nature was introduced in the 1970's without success. If such legislation is introduced again we will need strong Congressional support to obtain passage.

We are making improvements with respect to managing the various types of property we need to continue to own to accomplish our mission. A few examples are:

- Within OSD, management control of property is the responsibility of the Assistant Secretary Defense (Acquisition and Logistics). Financial and accounting responsibilities are with the Assistant Secretary Defense (Comptroller).
- The Defense Government Property Council (DGPC) has been strengthened under new OSD leadership -- I am chairing the council with other OSD principals being Mr. Shriber, DASD (Logistic and Materiel Management), OASD (Acquisition and Logistics); and Mr. Draft, DASD (Management Systems), OASD (Comptroller). The chairman of the Council's coordination committee, has been relocated to my immediate staff in the Pentagon to enhance daily coordination of all property actions within OSD and the services.

- The Navy formed a Navy Government Property Council in April, 1985, to serve as a focal point to centralize recommendations for policy improvement. We have been informed that the Army is planning to form an Army Government Property Council. These service councils should help in the implementation of Defense Government property policies.
- A modification to DODI 4140.48, titled "Controls of Access to DOD Material Inventories" has been signed by the ASD (A & L). This modification requires that GFM requisitions for production and supply contractors as well as maintenance contractors be submitted to a central office within each service for review and validation.
- An ad hoc group to the Defense Property Council is devising improved controls over Government property in the custody of contractors by developing a database for the use of property managers. This database is designed to provide managers with sufficient visibility to adequately manage the Government owned assets that are under their responsibility. The system being developed is called the: Department of Defense Industrial Property Management System. Current plans are to have the ad hoc group display this system to the property council during June 1986. I have been informed that its accountability subsystem is being designed to track all dollars of DOD plant and equipment on a contract by contract basis and will require all dollars reported in one year to be accounted for in the following year. Accountability tracking of special test equipment, special tooling, military property, and material would be phased-in over time -- first through the GOCO's and plant representative offices (which account for over 75 percent of the Dollars) where we have direct physical access to the contractors' records on a daily basis. It appears this additional reporting can be accomplished at the GOCO's without contractual changes or additional report-approval authorities. Phasing-in of additional reporting by contractor owned and operated plants will probably take more time since existing contracts will have to be modified and OMB report approval clearances obtained.
- The Defense Logistics Agency (DLA) is disposing of over 6,000 idle and unneeded industrial plant equipment items from the DOD General Reserve. This disposal will take approximately three years since the sales have been constrained by the Department of Commerce in order to eliminate a market impact on commercial machine tool sales.

- The Property Council's ad hoc group for financial accounting for Government property has been working to expedite implementation of financial accounting standards for property. Since we came before your committee last year our accountants identified a candidate system for potential DOD-wide use. Efforts are ongoing to evaluate the suitability of the system in terms of the management needs and overall financial systems of each of the services. The candidate system is in use by Air Force Industrial Funds and plans have been developed to upgrade the system so that it can be used by non-industrial fund users. Current Air Force planning schedules call for the upgraded system to be operational during October, 1987.

We are particularly pleased with the system because it has widespread acceptance by contractors; and this was a major industry concern when we were discussing the need for a financial accounting system to control GFM, and the related concepts.

We believe that the Air Force system, and the modifications that are being made to it, represent the best approach to accounting for GFM that has been demonstrated. The other DOD components have been exposed to the Air Force accounting system and were requested to consider it for adoption. We believe making use of accounting systems already developed makes good sense -- it is often less costly to adopt techniques and technologies of existing systems rather than designing new ones.

In conclusion, we have seen progress during the past year in property. However, we are aware that the following areas, as well as others, need continued attention and strengthening:

- Facilities phasedown;
- Negotiated sale of GOCO's;
- Reduction of initial provisioning of equipment;

- Implementation of financial accounting; and
- Increased visibility of property in the possession of contractors.

My office, as well as the Defense Government Property Council will continue to monitor and strengthen the government property program and we are committed to initiate policy changes as necessary.

As previously stated, we look to the private sector to provide the vast majority of capital assets that are necessary to manufacture defense goods. Our industrial preparedness needs will require us to continue some ownership. We are committed to reducing this ownership to the essential nucleus intended by the Defense Industrial Reserve Act of 1973.

This concludes my prepared statement. Representatives from the services, the Defense Logistics Agency, and I are available to respond to any questions you may have.

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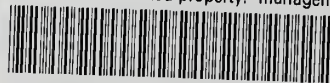
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